

BIMINI CAPITAL MANAGEMENT, INC.
Form 10-K
March 09, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011

Commission File Number: 001-32171

Bimini Capital Management, Inc.
(Exact name of registrant as specified in its charter)

Maryland
(State or other jurisdiction of
incorporation or organization)

72-1571637
(I.R.S. Employer
Identification No.)

3305 Flamingo Drive, Vero Beach, Florida 32963
(Address of principal executive offices) (Zip Code)

(772) 231-1400
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act:

Title of Each Class
Class A Common Stock, \$0.001 par value

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Edgar Filing: BIMINI CAPITAL MANAGEMENT, INC. - Form 10-K

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer
 Smaller Reporting Company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes No

State the aggregate market value of the voting stock held by non-affiliates of the Registrant as of June 30, 2011:

Title of each Class	Shares held by non-affiliates	Aggregate market value held by non-affiliates
Class A Common Stock, \$0.001 par value	8,627,622	\$ 6,300,000 (a)
Class B Common Stock, \$0.001 par value	20,760	\$ 1,000 (b)
Class C Common Stock, \$0.001 par value	31,938	\$ 1,500 (b)

(a) The aggregate market value was calculated by using the last sale price of the Class A Common Stock as of June 30, 2011.

(b) The market value of the Class B and Class C Common Stock is an estimate based on their initial purchase price.

Indicate the number of shares outstanding of each of the Registrant's classes of common stock, as of the latest practicable date:

Title of each Class	Latest Practicable Date	Shares Outstanding
Class A Common Stock, \$0.001 par value	March 9, 2012	10,086,854
Class B Common Stock, \$0.001 par value	March 9, 2012	31,938
Class C Common Stock, \$0.001 par value	March 9, 2012	31,938

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement for its 2012 Annual Meeting of Stockholders to be held on Tuesday, June 5, 2012 are incorporated by reference into Part III of this Annual Report on Form 10-K.

BIMINI CAPITAL MANAGEMENT, INC.

INDEX

PART I

ITEM 1. Business.	1
ITEM 1A. Risk Factors	29
ITEM 1B. Unresolved Staff Comments.	48
ITEM 2. Properties.	49
ITEM 3. Legal Proceedings.	49
ITEM 4. Mine Safety Disclosure.	50

PART II

ITEM 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities.	51
ITEM 6. Selected Financial Data.	53
ITEM 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.	54
ITEM 7A. Quantitative and Qualitative Disclosures About Market Risk.	69
ITEM 8. Financial Statements and Supplementary Data.	70
ITEM 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure.	101
ITEM 9A. Controls and Procedures.	101
ITEM 9B. Other Information.	104

PART III

ITEM 10. Directors, Executive Officers and Corporate Governance.	105
ITEM 11. Executive Compensation.	105
ITEM 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.	105
ITEM 13. Certain Relationships and Related Transactions, and Director Independence.	105
ITEM 14. Principal Accountant Fees and Services.	105

PART IV

ITEM 15. Exhibits, Financial Statement Schedules.	106
---------------------------------------------------	-----

PART I

ITEM 1. BUSINESS

Overview

Bimini Capital Management, Inc., a Maryland corporation (“Bimini Capital” and, collectively with its subsidiaries, the “Company,” “we” or “us”), is primarily in the business of investing in mortgage-backed securities. We are organized and operate as a real estate investment trust, or “REIT”, for federal income tax purposes, and our corporate structure includes a qualified REIT subsidiary, Orchid Island Capital, Inc. (“Orchid”), and two taxable REIT subsidiaries (“TRS”). Bimini Capital’s website is located at <http://www.biminicapital.com>.

From November 3, 2005 to June 30, 2007, we operated a mortgage banking business through a TRS. This entity ceased originating mortgages through two of their production channels during the second quarter of 2007 and the third, the retail loan production channel, was sold. No mortgage loans were originated after June 30, 2007.

History

We were originally formed in September 2003 as Bimini Mortgage Management, Inc. (“Bimini Mortgage”) for the purpose of creating and managing a leveraged investment portfolio consisting of residential mortgage-backed securities (“MBS”). Through November 2, 2005, we operated solely as a REIT.

- On November 3, 2005, Bimini Mortgage acquired Opteum Financial Services, LLC (“OFS”). Upon closing of the transaction, OFS became a wholly-owned taxable REIT subsidiary of the Company. This entity was renamed Orchid Island TRS, LLC (“OITRS”) effective July 3, 2007 and then renamed MortCo TRS, LLC (“MortCo”) effective March 8, 2011. Hereinafter, any historical mention, discussion or references to Opteum Financial Services, LLC, Orchid Island TRS, LLC, OFS or to OITRS (such as in previously filed documents or Exhibits) now means MortCo.
 - On February 10, 2006, Bimini Mortgage changed its name to Opteum Inc. (“Opteum”).
- On April 18, 2007, the Board of Managers of MortCo, at the recommendation of the Board of Directors of the Company, approved the closure of MortCo’s wholesale and conduit mortgage loan origination channels in the second quarter of 2007. Also, during the second and third quarters of 2007, substantially all of the other operating assets of MortCo were sold and the proceeds were primarily used to repay secured indebtedness.
 - On September 28, 2007, Opteum changed its name to Bimini Capital Management, Inc.

Structure

Bimini Capital and Orchid have elected to be taxed as a REIT under the Internal Revenue Code of 1986, as amended (the “Code”). Our qualification as a REIT depends upon our ability to meet, on an annual or in some cases quarterly basis, various complex requirements under the Internal Revenue Code relating to, among other things, the sources of our gross income, the composition and values of our assets, our distribution levels and the diversity of ownership of our shares. MortCo has been treated as a TRS since its acquisition, and is taxed separately from the REIT. Bimini Advisors, Inc. (“Bimini Advisors”) is a TRS incorporated in 2011, and its activities were insignificant.

As used in this document, discussions related to “Bimini Capital,” the parent company, the registrant, and the REIT qualifying activities or the general management of our portfolio of MBS refer to Bimini Capital Management, Inc. and its qualified REIT subsidiary. Further, discussions related to our taxable REIT subsidiary or non-REIT eligible assets refer to MortCo and its consolidated subsidiaries and Bimini Advisors. Discussions relating to the “Company” refer to the consolidated entity (the combination of Bimini Capital, its qualified REIT subsidiary, MortCo and its subsidiaries and Bimini Advisors).

Description of Our Business

Investment Objective

We manage a portfolio of agency MBS and structured MBS. We intend to generate income derived from the net interest margin of our MBS portfolio, levered predominantly under repurchase agreement funding, net of associated hedging costs, and the interest income derived from our unlevered portfolio of structured MBS. We seek to minimize the volatility of both the income generated by our portfolio and the value of our portfolio of securities through our capital allocation, asset selection, interest rate risk management and liquidity management. However, there can be no assurance we will be able to do so consistently, or at all. Our Board of Directors may change our investment strategy without prior notice to you or a vote of our stockholders.

Portfolio Composition

The primary assets in our current portfolio of mortgage related securities are fixed-rate MBS, adjustable-rate MBS (“ARM’s”), hybrid adjustable-rate MBS (“hybrid ARM’s”) and structured MBS. The primary structured MBS in our portfolio are interest only and inverse interest only securities, although we may also employ other types of structured MBS. The mortgage related securities we acquire are obligations issued by federal agencies or federally chartered entities, primarily Fannie Mae, Freddie Mac and Ginnie Mae.

We seek to own securities with well documented and understood prepayment histories and characteristics, with the investment goal of minimizing the volatility of our earnings resulting from the effect of volatile prepayments of the mortgage loans underlying our securities. Our diversified portfolio will generally be comprised of a high percentage of securities with borrower and/or loan characteristics that we expect will result in lower sensitivity to available refinancing incentives. Examples would be pools of MBS collateralized by mortgages with lower loan balances, newly originated fixed-rate and hybrid ARM securities or lower coupon mortgages, among others. We may also own securities with higher sensitivity to available refinancing incentives, but in both cases we seek securities with prepayment characteristics that are more predictable.

Borrowers with low loan balances have a lower economic incentive to refinance and have historically prepaid at lower rates than borrowers with larger loan balances. The reduced incentive to refinance is caused by two factors: borrowers with low loan balances will have smaller interest savings because overall interest payments are smaller on their loans; and closing costs for refinancings, which are generally not proportionate to the size of a loan, make refinancing of smaller loans less attractive as it takes a longer period of time for the interest savings to cover the cost of refinancing.

Agency pools collateralized by newly originated loans generally experience slower prepayments because borrowers are required to pay fees each time they originate a new loan or refinance an existing one and, absent material changes in prevailing interest rates, the out-of-pocket costs discourage the borrower from refinancing. Typically such costs are recouped over time by way of interest cost savings. Loans to borrowers with low relative interest rates tend to refinance less often simply because they have little or no economic incentive to do. Prepayments on such loans tend to be limited to instances where the borrower moves and sells the property, thus resulting in an early prepayment of the loan.

Our structured MBS will generally be collateralized by loans similar to those described above. However, securities such as interest only or inverse interest only securities receive cash flows associated with the interest paid by the underlying loans, and do not entitle the holder to receive any principal payments. Also, inverse interest only securities have coupon rates that are affected by the level of one month London Interbank Offered Rate (“LIBOR”), and will move in the opposite direction of LIBOR. Accordingly, when LIBOR goes up, the coupon on such securities will go down, and vice versa.

We have created and will attempt to maintain a diversified portfolio to avoid undue geographic, loan originator, and other types of concentrations. By maintaining essentially all of our assets in government or government-sponsored or chartered enterprises and government or federal agencies, which now carry a more explicit guarantee of the federal government as to payment of principal and interest, we believe we can significantly reduce our exposure to losses from credit risk. We intend to acquire assets that will enable us to be exempt from the Investment Company Act of 1940.

Legislation may be proposed to change the relationship between certain agencies, such as Fannie Mae and the federal government. This may have the effect of reducing the actual or perceived credit quality of mortgage related securities issued by these agencies. As a result, such legislation could increase the risk of loss on investments in Fannie Mae and/or Freddie Mac MBS. We currently intend to continue to invest in such securities, even if such agencies' relationships with the federal government change.

Capital Allocation Strategy

We intend to deploy our capital using two core strategies, which are to create and maintain a levered MBS portfolio and an unlevered structured MBS portfolio. The leverage applied to the MBS portfolio will typically be less than twelve to one. The capital applied to the two portfolios will vary over time and will be managed in an effort to maintain not only the level of income generated by the combined portfolios, but also the stability of the income stream, to the extent we can do so. Capital will be allocated so as to assist management in attempts to maintain the stability of the value of the combined portfolios. Typically, but not always, structured MBS and PT MBS exhibit materially different sensitivities to movements in interest rates, and to the extent they do so, may protect us against declines in the market value of our combined portfolio. However, there can be no assurance that management will be able to achieve such stability consistently, or at all. Finally, we will allocate our capital between the two strategies so as to assist with our interest rate risk management efforts with respect to the levered portfolio and our liquidity management. The unlevered portfolio does not require unencumbered cash or cash equivalents to be maintained so as to meet price related margin calls associated with our repo borrowings. To the extent more capital is deployed in the unlevered portfolio, our liquidity needs will generally be less.

We intend to continue to maintain our status as a REIT and operate in a manner that will not subject us to regulation under the Investment Company Act of 1940. In order to avoid being subject to regulation under the Investment Company Act, we must maintain at least 55% of our assets in qualifying real estate assets (the “Investment Company Test”). For purposes of this test, structured MBS are non-qualifying real estate assets. Accordingly, while we have no explicit limitation on the amount of our capital we will deploy to the unlevered structured MBS portfolio, we will deploy our capital in such a way so as to avoid regulation under the Investment Company Act.

Interest Rate Risk Management – Levered MBS Portfolio

We believe the primary risk inherent in our investments is the effect of movements in interest rates. This risk arises because the effects of interest rate changes on our borrowings differ from the effects of interest rate changes on the income from, or value of, our investments. We therefore follow an interest rate risk management program designed to

offset the potential adverse effects resulting from the rate adjustment limitations on our mortgage related securities. We seek to minimize differences between interest rate indices and interest rate adjustment periods of our adjustable-rate mortgage-backed securities and related borrowings by matching the terms of assets and related liabilities both as to maturity and to the underlying interest rate index used to calculate interest rate charges.

- 3 -

Our interest rate risk management program encompasses a number of procedures, including the following:

- Monitoring and adjusting, if necessary, the interest rate sensitivity of our mortgage related securities compared with the interest rate sensitivities of our borrowings.
- Attempting to structure our repurchase agreements that fund our purchases of PT MBS to have a range of different maturities and interest rate adjustment periods. We attempt to structure these repurchase agreements to match the reset dates on our PT MBS when possible. At December 31, 2011, the weighted average months to reset of our adjustable-rate mortgage-backed securities was 65.8 months and the weighted average reset on the corresponding repurchase agreements was 25 days; and
- Actively managing, on an aggregate basis, the interest rate indices and interest rate adjustment periods of our mortgage related securities compared to the interest rate indices and adjustment periods of our borrowings. Our liabilities under our repurchase agreements are all LIBOR-based, and we, among other considerations, select our adjustable-rate mortgage-backed securities to favor LIBOR indexes.

As a result, we expect to be able to adjust the average maturities and reset periods of our borrowings on an ongoing basis by changing the mix of maturities and interest rate adjustment periods as borrowings mature or are renewed. Through the use of these procedures, we attempt to reduce the risk of differences between interest rate adjustment periods of our adjustable-rate mortgage-backed securities and our related borrowings.

We may from time to time use derivative financial instruments to hedge all or a portion of the interest rate risk associated with our borrowings. We may enter into swap or cap agreements, option, put or call agreements, futures contracts, forward rate agreements or similar financial instruments to hedge indebtedness that we may incur. These contracts would be intended to more closely match the effective maturity of, and the interest received on, our assets with the effective maturity of, and the interest owed on, our liabilities. However, no assurances can be given that interest rate risk management strategies can successfully be implemented.

Structured MBS in our unlevered portfolio generally exhibit sensitivities to movements in interest rates that are different than the securities we typically own in our levered portfolio; to the extent this occurs, it may provide some protection against declines in the market value of our combined portfolio that result from adverse interest rate movements. The inability to match closely the maturities and interest rates of our assets and liabilities, or the inability to protect adequately against declines in the market value of our assets, could result in losses.

Liquidity Management Strategy

As a result of our extensive use of leverage, we must manage our portfolio and operations so as to maintain the liquidity needed to meet price related margin calls associated with the assets pledged to obtain such leverage. This is accomplished by the following measures:

- Owning securities with lower anticipated levels of prepayments so as to avoid excessive margin calls when monthly prepayments are announced. Prepayment speeds are typically made available prior to the receipt of the related cash flows, thus causing the market value of the related security to decrease prior to the receipt of the associated cash. This gives rise to a temporary collateral deficiency and generally results in margin calls by lenders.

- Maintaining larger balances of cash or unencumbered assets to meet margin calls.

-

Proactively making margin calls on our credit counterparties when we have an excess of collateral pledged against our borrowings by actively monitoring the asset prices and collateral levels for assets pledged against such borrowings.

- Reducing our leverage.
- Redeploying capital from our levered MBS portfolio to our unlevered structured MBS portfolio.
- Obtaining funding arrangements whereby prepayment related margin calls are deferred or waived in exchange for payments to the lender tied to the dollar amount of the collateral deficiency and a pre-determined interest rate.

While our current financial condition prohibits us from obtaining funding arrangements whereby capital deficiency related margin calls can be deferred or waived, we continue to employ all of the measures detailed above so as to maintain our liquidity.

Repurchase Agreement Trading, Clearing and Administrative Services

We have engaged AVM, L.P. (a securities broker-dealer) to provide us with repurchase agreement trading, clearing and administrative services. AVM acts as our clearing agent and adviser in arranging for third parties to enter into repurchase agreements with us, executes and maintains records of our repurchase transactions and assists in managing the margin arrangements between us and our counterparties for each of our repurchase agreements.

Description of Mortgage Related Securities

Mortgage-Backed Securities

Pass-Through Certificates. We intend to invest in PT certificates, which are securities representing interests in pools of mortgage loans secured by residential real property in which payments of both interest and principal on the securities are generally made monthly. In effect, these securities pass-through the monthly payments made by the individual borrowers on the mortgage loans that underlie the securities, net of fees paid to the issuer or guarantor of the securities. PT certificates can be divided into various categories based on the characteristics of the underlying mortgages, such as the term or whether the interest rate is fixed or variable.

A key feature of most mortgage loans is the ability of the borrower to repay principal earlier than scheduled. This is called a prepayment. Prepayments arise primarily due to sale of the underlying property, refinancing, or foreclosure. Prepayments result in a return of principal to pass-through certificate holders. This may result in a lower or higher rate of return upon reinvestment of principal. This is generally referred to as prepayment uncertainty. If a security purchased at a premium prepays at a higher-than-expected rate, then the value of the premium would be eroded at a faster-than-expected rate. Similarly, if a discount mortgage prepays at a lower-than-expected rate, the amortization towards par would be accumulated at a slower-than-expected rate. The possibility of these undesirable effects is sometimes referred to as "prepayment risk."

In general, declining interest rates tend to increase prepayments, and rising interest rates tend to slow prepayments. Like other fixed-income securities, when interest rates rise, the value of mortgage related securities generally declines. The rate of prepayments on underlying mortgages will affect the price and volatility of mortgage related securities and may shorten or extend the effective maturity of the security beyond what was anticipated at the time of purchase. If interest rates rise, our holdings of mortgage related securities may experience reduced returns if the borrowers of the underlying mortgages pay off their mortgages later than anticipated. This is generally referred to as extension risk.

The payment of principal and interest on mortgage PT securities issued by Ginnie Mae, but not the market value, is guaranteed by the full faith and credit of the federal government. Payment of principal and interest on mortgage PT certificates issued by Fannie Mae and Freddie Mac, but not the market value, is guaranteed by the respective agency

issuing the security.

- 5 -

The mortgage loans underlying PT certificates can generally be classified in the following five categories:

- **Fixed-Rate Mortgages.** As of December 31, 2011, 38.9% of our portfolio consisted of fixed-rate MBS. Fixed-rate mortgages are those where the borrower pays an interest rate that is constant throughout the term of the loan. Traditionally, most fixed-rate mortgages have an original term of 30 years. However, shorter terms (also referred to as final maturity dates) have become common in recent years. Because the interest rate on the loan never changes, even when market interest rates change, over time there can be a divergence between the interest rate on the loan and current market interest rates. This in turn can make a fixed-rate mortgages price sensitive to market fluctuations in interest rates. In general, the longer the remaining term on the mortgage loan, the greater the price sensitivity.
- **Collateralized Mortgage Obligations.** As of December 31, 2011, we held no collateralized mortgage obligations in our portfolio. Collateralized mortgage obligations, or CMOs, are a type of MBS. Interest and principal on a CMO are paid, in most cases, on a monthly basis. CMOs may be collateralized by whole mortgage loans, but are more typically collateralized by portfolios of mortgage pass-through securities issued directly by or under the auspices of Ginnie Mae, Freddie Mac or Fannie Mae. CMOs are structured into multiple classes, with each class bearing a different stated maturity. Monthly payments of principal, including prepayments, are first returned to investors holding the shortest maturity class. Investors holding the longer maturity classes receive principal only after the first class has been retired. Generally, fixed-rate mortgages are used to collateralize CMOs. However, the CMO tranches need not all have fixed-rate coupons. Some CMO tranches have floating rate coupons that adjust based on market interest rates, subject to some limitations. Such tranches, often called "CMO floaters," can have relatively low price sensitivity to interest rates.
- **Adjustable-Rate Mortgages.** As of December 31, 2011, 13.4% of our portfolio consisted of adjustable-rate mortgage-backed securities ("ARMs"). ARMs, are those for which the borrower pays an interest rate that varies over the term of the loan. The interest rate usually resets based on market interest rates, although the adjustment of such an interest rate may be subject to certain limitations. Traditionally, interest rate resets occur at regular set intervals (for example, once per year). We will refer to such ARMs as "traditional" ARMs. Because the interest rates on ARMs fluctuate based on market conditions, ARMs tend to have interest rates that do not deviate from current market rates by a large amount. This in turn can mean that ARMs have less price sensitivity to interest rates.
- **Hybrid Adjustable-Rate Mortgages.** As of December 31, 2011, 27.9% of our portfolio consisted of hybrid ARMs. Hybrid ARMs have a fixed-rate for the first few years of the loan, often three, five, or seven years, and thereafter reset periodically like a traditional ARM. Effectively such mortgages are hybrids, combining the features of a pure fixed-rate mortgage and a "traditional" ARM. Hybrid ARMs have price sensitivity to interest rates similar to that of a fixed-rate mortgage during the period when the interest rate is fixed and similar to that of an ARM when the interest rate is in its periodic reset stage. However, because many hybrid ARMs are structured with a relatively short initial time span during which the interest rate is fixed, even during that segment of its existence, the price sensitivity may be high.
- **Balloon Maturity Mortgages.** As of December 31, 2011, we held no balloon maturity MBS in our portfolio. Balloon maturity mortgages are a type of fixed-rate mortgage where all or most of the principal amount is due at maturity, rather than paid down, or amortized, over the life of the loan. These mortgages have a static interest rate for the life of the loan. However, the term of the loan is usually quite short, typically less than seven years. As the balloon maturity mortgage approaches its maturity date, the price sensitivity of the mortgage declines.

- Interest Only Securities (“IO”). As of December 31, 2011, 7.7% of our portfolio consisted of IO securities. IO securities represent the stream of interest payments on a pool of mortgages, either fixed-rate mortgages or hybrid ARMs; holders of IO securities have no claim to any principal payments. The value of IOs depends primarily on two factors: prepayments and interest rates. Prepayments on the underlying pool of mortgages reduce the stream of interest payments going forward, hence IOs are highly sensitive to the rate at which the mortgages in the pool are prepaid. IOs are also sensitive to changes in interest rates. An increase in interest rates reduces the present value of future interest payments on a pool of mortgages. On the other hand, an increase in interest rates has a tendency to reduce prepayments, which increases the expected absolute amount of future interest payments.
- Inverse Interest Only Securities (“IIO”). As of December 31, 2011, 12.1% of our portfolio consisted of IIO securities. IIO securities represent the stream of interest payments on a pool of mortgages, either fixed-rate mortgages or hybrid adjustable-rate mortgages; holders of IIO securities have no claim to any principal payments. The value of IIOs depends primarily on three factors; prepayments, LIBOR rates and term interest rates. Prepayments on the underlying pool of mortgages reduce the stream of interest payments; hence IIOs are highly sensitive to the rate at which the mortgages in the pool are prepaid. The coupon on IIO securities is derived from both the coupon interest rate on the underlying pool of mortgages and one month LIBOR. IIO securities are typically created in conjunction with a floating rate CMO which has a principal balance and which is entitled to receive all of the principal payments on the underlying pool of mortgages. The coupon on the floating rate CMO is also based on one month LIBOR. Typically, the coupon on the floating rate CMO and the IIO, when combined, equal the coupon on the pool of underlying mortgages. The coupon on the pool of underlying mortgages typically represents a cap or ceiling on the combined coupons of the floating rate CMO and the IIO. Accordingly, when the value of one month LIBOR increases, the coupon of the floating rate CMO will increase and the coupon on the IIO will decrease. When the value of one month LIBOR falls, the opposite is true. Accordingly, the value of IIO securities are sensitive to the level of one month LIBOR and expectations by market participants of future movements in the level of one month LIBOR. IIO securities are also sensitive to changes in interest rates. An increase in interest rates reduces the present value of future interest payments on a pool of mortgages. On the other hand, an increase in interest rates has a tendency to reduce prepayments, which increases the expected absolute amount of future interest payments.
- Principal Only Securities (“PO”). As of December 31, 2011, we held no PO securities in our portfolio. PO securities represent the stream of principal payments on a pool of mortgages; holders of PO securities have no claim to any interest payments, although the ultimate amount of principal to be received over time is known – it equals the principal balance of the underlying pool of mortgages. What is not known is the timing of the receipt of the principal payments. The value of POs depends primarily on two factors; prepayments and interest rates. Prepayments on the underlying pool of mortgages accelerate the stream of principal repayments; hence POs are highly sensitive to the rate at which the mortgages in the pool are prepaid. POs are also sensitive to changes in interest rates. An increase in interest rates reduces the present value of future principal payments on a pool of mortgages. Further, an increase in interest rates also has a tendency to reduce prepayments, which decelerates, or pushes further out in time, the ultimate receipt of the principal payments. The opposite is true when interest rates decline.

The following table shows the breakdown of mortgage loans underlying our MBS portfolio as of December 31, 2011 and 2010:

(in thousands)

	December 31,			
	2011		2010	
	Carrying Value	% of Total	Carrying Value	% of Total
Pass-Through Certificates:				
Adjustable-rate Mortgages	\$12,181	13.4	\$64,458	47.7
Fixed-rate Mortgages	35,417	38.9	50,013	37.0
Hybrid ARMs	25,466	27.9	2,783	2.1
Total Pass-Through Certificates	73,064	80.2	117,254	86.8
Structured Mortgage Certificates:				
Interest Only MBS	7,074	7.7	4,772	3.5
Inverse IO MBS	11,004	12.1	13,107	9.7
Total Structured Mortgage Certificates	18,078	19.8	17,879	13.2
Totals	\$91,142	100.0	\$135,133	100.0

As of December 31, 2011, 64.3%, 29.9% and 5.8% of our portfolio was issued by Fannie Mae, Freddie Mac and Ginnie Mae, respectively. As of December 31, 2011, our portfolio had a weighted average coupon of 4.37%. The constant prepayment rate (CPR) for the portfolio, which reflects the annualized proportion of principal that was prepaid, was 29.01% for December 2011. The effective duration for the portfolio was (3.492) as of December 31, 2011. Duration measures the price sensitivity of a fixed income security to movements in interest rates. Effective duration captures both the movement in interest rates and the fact that the cash flows of a mortgage related security are altered when interest rates move.

CERTAIN FEDERAL INCOME TAX CONSIDERATIONS

The following discussion describes the material federal income tax consequences to stockholders of the acquisition, ownership and disposition of our Class A Common Stock. The tax treatment of stockholders will vary depending upon the stockholder's particular situation, and this discussion addresses only stockholders that hold shares of our common stock as a capital asset for U.S. federal income tax purposes and does not address all aspects of taxation that may be relevant to particular stockholders in light of their personal investment or tax circumstances. This section also does not address all aspects of taxation that may be relevant to certain types of stockholders to which special provisions of the federal income tax laws apply, including:

- dealers in securities or currencies;
- traders in securities that elect to use a mark-to-market method of accounting for their securities holdings;
- banks;
- tax-exempt organizations (except to the extent described below in “— Taxation of Tax-Exempt Stockholders”);
- certain insurance companies;

- persons liable for the alternative minimum tax;
- persons that hold common stock as a hedge against interest rate or currency risks or as part of a straddle or conversion transaction; and

- stockholders whose functional currency is not the U.S. dollar.

This summary is based on the Code, its legislative history, existing and proposed regulations under the Code, published rulings and court decisions. This summary describes the provisions of these sources of law in a general manner, and as they are currently in effect. All of these sources of law may change at any time, and any change in the law may apply retroactively.

Taxation of Holders of our Class A Common Stock

The following is a summary of certain federal income tax considerations with respect to the acquisition, ownership and disposition of our Class A Common Stock.

We urge each stockholder to consult with their own tax advisor regarding the specific tax consequences to them of the ownership and disposition of our Class A Common Stock and of our election to be taxed as a REIT, specifically regarding the federal, state, local, foreign, and other tax consequences of such ownership, disposition and election, and regarding potential changes in applicable tax laws.

Taxation of Our Company

We elected to be taxed as a REIT under the federal income tax laws commencing with our initial short taxable year ended on December 31, 2003. We believe that we are organized and we have operated in such a manner so as to qualify for taxation as a REIT under the federal income tax laws, and we intend to continue to operate in such a manner, but no assurance can be given that we will operate in a manner so as to remain qualified as a REIT. This section discusses, in a general manner, the laws governing the federal income tax treatment of a REIT. These laws are highly technical and complex.

As a REIT, we generally will not be subject to federal income tax on the REIT taxable income that we distribute to our stockholders. The benefit of that tax treatment is that it avoids the double taxation, or taxation at both the corporate and stockholder levels, that generally applies to distributions by a corporation to its stockholders. However, we will be subject to federal tax in the following circumstances:

- We will pay federal income tax on taxable income, including net capital gain, that we do not distribute to stockholders during, or within a specified time period after, the calendar year in which the income is earned.
- We may be subject to the “alternative minimum tax” on any items of tax preference that we do not distribute or allocate to stockholders.
 - We will pay income tax at the highest corporate rate on:
 - net income from the sale or other disposition of property acquired through foreclosure, or foreclosure property, that we hold primarily for sale to customers in the ordinary course of business, and
 - other non-qualifying income from foreclosure property.
 - We will pay a 100% tax on our net income from sales or other dispositions of property, other than foreclosure property, that we hold primarily for sale to customers in the ordinary course of business.

- If we fail to satisfy the 75% gross income test or the 95% gross income test, as described below under “— Requirements for Qualification — Gross Income Tests,” and nonetheless continue to qualify as a REIT because we meet other requirements, we will pay a 100% tax on:

- 9 -

- the greater of (i) the amount by which we fail the 75% gross income test or (ii) the amount by which 95% of our gross income exceeds the amount of our income qualifying under the 95% gross income test, multiplied by
 - a fraction intended to reflect our profitability.
- In the event of a more than de minimis failure of any of the asset tests, as described below under “—Requirement for Qualification — Asset Tests,” as long as the failure was due to reasonable cause and not to willful neglect, we file a description of the assets that caused such failure with the IRS, and we dispose of the assets or otherwise comply with the asset tests within six months after the last day of the quarter in which we identify such failure, we will pay a tax equal to the greater of \$50,000 or 35% of the net income from the nonqualifying assets during the period in which we failed to satisfy any of the asset tests.
- In the event of a failure to satisfy one or more requirements for REIT qualification, other than the gross income tests or the asset tests, as long as such failure was due to reasonable cause and not to willful neglect, we will be required to pay a penalty of \$50,000 for each such failure.
- We will pay a 4% nondeductible excise tax on the excess of the required distribution over the amount we actually distributed if we fail to distribute during a calendar year at least the sum of:
 - 85% of our REIT ordinary income for the year,
 - 95% of our REIT capital gain net income for the year, and
 - any undistributed taxable income required to be distributed from earlier periods,
- We may elect to retain and pay income tax on our net long-term capital gain. In that case, a U.S. stockholder would be taxed on its proportionate share of our undistributed long-term capital gain (to the extent that we make a timely designation of such gain to the stockholder) and would receive a credit or refund for its proportionate share of the tax we paid.
- We will be subject to a 100% excise tax on transactions between us and a TRS that are not conducted on an arm’s-length basis.
- If we acquire any asset from a C corporation, or a corporation that generally is subject to full corporate-level tax, in a merger or other transaction in which we acquire a basis in the asset that is determined by reference either to the C corporation’s basis in the asset or to another asset, we will pay tax at the highest regular corporate rate applicable if we recognize gain on the sale or disposition of the asset during the 10-year period after we acquire the asset. The amount of gain on which we will pay tax is the lesser of:
 - the amount of gain that we recognize at the time of the sale or disposition, and
 - the amount of gain that we would have recognized if we had sold the asset at the time we acquired it.
- If we own a residual interest in a real estate mortgage investment conduit, or (“REMIC”), we will be taxed at the highest corporate rate on the portion of any excess inclusion income that we derive from the REMIC residual interests equal to the percentage of our stock that is held by “disqualified organizations.” Similar rules may apply if we own an equity interest in a taxable mortgage pool. To the extent that we own a REMIC residual interest or an equity interest in a taxable mortgage pool through a TRS, we will not be subject to this tax. For a discussion of

“excess inclusion income,” see “—Requirements for Qualification —Taxable Mortgage Pools.” A “disqualified organization” includes:

- 10 -

- the United States;
- any state or political subdivision of the United States;
 - any foreign government;
 - any international organization;
- any agency or instrumentality of any of the foregoing;
- any other tax-exempt organization, other than a farmer’s cooperative described in section 521 of the Code, that is exempt both from income taxation and from taxation under the unrelated business taxable income provisions of the Code; and
 - any rural electrical or telephone cooperative.

We do not currently hold, and do not intend to hold, REMIC residual interests or equity interests in taxable mortgage pools, at the REIT level.

Requirements for Qualification

Organizational Requirements

A REIT is a corporation, trust, or association that meets each of the following requirements:

- (1) It is managed by one or more trustees or directors.
- (2) Its beneficial ownership is evidenced by transferable shares, or by transferable certificates of beneficial interest.
- (3) It would be taxable as a domestic corporation, but for the REIT provisions of the federal income tax laws.
- (4) It is neither a financial institution nor an insurance company subject to special provisions of the federal income tax laws.
 - (5) At least 100 persons are beneficial owners of its shares or ownership certificates.
- (6) Not more than 50% in value of its outstanding shares or ownership certificates is owned, directly or indirectly, by five or fewer individuals, which the federal income tax laws define to include certain entities, during the last half of any taxable year.
- (7) It elects to be a REIT, or has made such election for a previous taxable year, and satisfies all relevant filing and other administrative requirements established by the IRS that must be met to elect and maintain REIT status.
- (8) It meets certain other qualification tests, described below, regarding the nature of its income and assets and the distribution of its income.

We must meet requirements 1 through 4 during our entire taxable year and must meet requirement 5 during at least 335 days of a taxable year of 12 months, or during a proportionate part of a taxable year of less than 12 months. Requirements 5 and 6 applied to us beginning with our 2004 taxable year. If we comply with all the requirements for ascertaining the ownership of our outstanding stock in a taxable year and have no reason to know that we violated requirement 6, we will be deemed to have satisfied requirement 6 for that taxable year. For purposes of determining share ownership under requirement 6, an “individual” generally includes a supplemental unemployment compensation benefits plan, a private foundation, or a portion of a trust permanently set aside or used exclusively for charitable purposes. An “individual,” however, generally does not include a trust that is a qualified employee pension or profit sharing trust under the federal income tax laws, and beneficiaries of such a trust will be treated as holding our stock in proportion to their actuarial interests in the trust for purposes of requirement 6.

We believe that we have issued sufficient stock with sufficient diversity of ownership to satisfy requirements 5 and 6. In addition, our charter restricts the ownership and transfer of our stock so that we should continue to satisfy these requirements.

Qualified REIT Subsidiaries. A corporation that is a “qualified REIT subsidiary” is not treated as a corporation separate from its parent REIT. All assets, liabilities, and items of income, deduction, and credit of a “qualified REIT subsidiary” are treated as assets, liabilities, and items of income, deduction, and credit of the REIT. A “qualified REIT subsidiary” is a corporation with all of the capital stock being owned by the REIT and that has not elected to be a TRS. Thus, in applying the requirements described herein, any “qualified REIT subsidiary” that we own will be ignored, and all assets, liabilities, and items of income, deduction, and credit of such subsidiary will be treated as our assets, liabilities, and items of income, deduction, and credit.

Other Disregarded Entities and Partnerships. An unincorporated domestic entity, such as a partnership, or limited liability company that has a single owner, generally is not treated as an entity separate from its parent for federal income tax purposes. An unincorporated domestic entity with two or more owners generally is treated as a partnership for federal income tax purposes. In the case of a REIT that is a partner in a partnership that has other partners, the REIT is treated as owning its proportionate share of the assets of the partnership and as earning its allocable share of the gross income of the partnership for purposes of the applicable REIT qualification tests. For purposes of the 10% value test (described in “— Asset Tests”), our proportionate share is based on our proportionate interest in the equity interests and certain debt securities issued by the partnership. For all of the other asset and income tests, our proportionate share is based on our proportionate interest in the capital interests in the partnership. Thus, our proportionate share of the assets, liabilities, and items of income of any partnership, joint venture, or limited liability company that is treated as a partnership for federal income tax purposes in which we acquire an interest, directly or indirectly, will be treated as our assets and gross income for purposes of applying the various REIT qualification requirements.

Taxable REIT Subsidiaries. A REIT is permitted to own up to 100% of the stock of one or more TRSs. A TRS is a fully taxable corporation that may earn income that would not be qualifying income if earned directly by the parent REIT. The subsidiary and the REIT must jointly elect to treat the subsidiary as a TRS. A corporation of which a TRS directly or indirectly owns more than 35% of the voting power or value of the stock will automatically be treated as a TRS. Overall, no more than 25% (20% for taxable years prior to 2009) of the value of a REIT’s assets may consist of stock or securities of one or more TRSs.

A TRS will pay income tax at regular corporate rates on any income that it earns. In addition, the TRS rules limit the deductibility of interest paid or accrued by a TRS to its parent REIT to assure that the TRS is subject to an appropriate level of corporate taxation. Further, the rules impose a 100% excise tax on transactions between a TRS and its parent REIT or the REIT’s tenants that are not conducted on an arm’s-length basis. We have elected to treat MortCo as a TRS. Our TRS is subject to corporate income tax on its taxable income. We believe that all transactions between us and our

TRS have been and will be conducted on an arm's-length basis.

Taxable Mortgage Pools. An entity, or a portion of an entity, may be classified as a taxable mortgage pool under the Code if:

- 12 -

- substantially all of its assets consist of debt obligations or interests in debt obligations;
- more than 50% of those debt obligations are real estate mortgage loans or interests in real estate mortgage loans as of specified testing dates;
 - the entity has issued debt obligations that have two or more maturities; and
- the payments required to be made by the entity on its debt obligations “bear a relationship” to the payments to be received by the entity on the debt obligations that it holds as assets.

Under U.S. Treasury regulations, if less than 80% of the assets of an entity (or a portion of an entity) consist of debt obligations, these debt obligations are considered not to comprise “substantially all” of its assets, and therefore the entity would not be treated as a taxable mortgage pool.

We may make investments or enter into financing and securitization transactions that give rise to our being considered to be, or to own an interest in, one or more taxable mortgage pools. Where an entity, or a portion of an entity, is classified as a taxable mortgage pool, it is generally treated as a taxable corporation for federal income tax purposes. However, special rules apply to a REIT, a portion of a REIT, or a qualified REIT subsidiary, that is a taxable mortgage pool. The portion of the REIT’s assets, held directly or through a qualified REIT subsidiary, that qualifies as a taxable mortgage pool is treated as a qualified REIT subsidiary that is not subject to corporate income tax, and the taxable mortgage pool classification does not affect the tax status of the REIT. Rather, the consequences of the taxable mortgage pool classification would generally, except as described below, be limited to the REIT’s stockholders. The Treasury Department has yet to issue regulations governing the tax treatment of the stockholders of a REIT that owns an interest in a taxable mortgage pool.

A portion of our income from a taxable mortgage pool arrangement, which might be non-cash accrued income, or “phantom” taxable income, could be treated as “excess inclusion income.” Excess inclusion income is an amount, with respect to any calendar quarter, equal to the excess, if any, of (i) income allocable to the holder of a REMIC residual interest or taxable mortgage pool interest over (ii) the sum of an amount for each day in the calendar quarter equal to the product of (a) the adjusted issue price at the beginning of the quarter multiplied by (b) 120% of the long-term federal rate (determined on the basis of compounding at the close of each calendar quarter and properly adjusted for the length of such quarter). This non-cash or “phantom” income is subject to the distribution requirements that apply to us and could therefore adversely affect our liquidity. See “— Distribution Requirements.”

Our excess inclusion income would be allocated among our stockholders. A stockholder’s share of excess inclusion income (i) would not be allowed to be offset by any net operating losses otherwise available to the stockholder, (ii) would be subject to tax as unrelated business taxable income in the hands of most types of stockholders that are otherwise generally exempt from federal income tax, and (iii) would result in the application of U.S. federal income tax withholding at the maximum rate (30%), without reduction for any otherwise applicable income tax treaty, to the extent allocable to most types of foreign stockholders. See “—Taxation of Tax-Exempt Stockholders” and “—Taxation of Non-U.S. Stockholders.” The manner in which excess inclusion income would be allocated among shares of different classes of our stock or how such income is to be reported to stockholders is not clear under current law. Tax-exempt investors, foreign investors, and taxpayers with net operating losses should carefully consider the tax consequences described above and are urged to consult their tax advisors in connection with their decision to invest in our stock.

If we were to own less than 100% of the ownership interests in an entity that is classified as a taxable mortgage pool, the foregoing rules would not apply. Rather, the entity would be treated as a corporation for federal income tax purposes, and its income would be subject to corporate income tax. In addition, this characterization would alter our REIT income and asset test calculations and could adversely affect our compliance with those requirements. We currently do not own, and currently do not intend to own, some, but less than all, of the ownership interests in an entity that is or will become a taxable mortgage pool, and we intend to monitor the structure of any taxable mortgage pools in which we have an interest to ensure that they will not adversely affect our status as a REIT.

Gross Income Tests

We must satisfy two gross income tests annually to maintain our qualification as a REIT. First, at least 75% of our gross income for each taxable year must consist of defined types of income that we derive, directly or indirectly, from investments relating to real property or mortgage loans on real property or qualified temporary investment income. Qualifying income for purposes of the 75% gross income test generally includes:

- rents from real property;
- interest on debt secured by a mortgage on real property, or on interests in real property;
- dividends or other distributions on, and gain from the sale of, shares in other REITs;
- gain from the sale of real estate assets;
- amounts, such as commitment fees, received in consideration for entering into an agreement to make a loan secured by real property, unless such amounts are determined by income and profits;
- income derived from a REMIC in proportion to the real estate assets held by the REMIC, unless at least 95% of the REMIC's assets are real estate assets, in which case all of the income derived from the REMIC; and
- income derived from the temporary investment of new capital that is attributable to the issuance of our stock or a public offering of our debt with a maturity date of at least five years and that we receive during the one-year period beginning on the date on which we received such new capital.

Second, in general, at least 95% of our gross income for each taxable year must consist of income that is qualifying income for purposes of the 75% gross income test, other types of interest and dividends, gain from the sale or disposition of stock or securities or any combination of these. Gross income from our sale of property that we hold primarily for sale to customers in the ordinary course of business is excluded from both the numerator and the denominator in both income tests. Income and gain from “hedging transactions,” as defined in “— Hedging Transactions,” that we entered into on or before July 30, 2008 to hedge indebtedness incurred or to be incurred to acquire or carry real estate assets and that are clearly and timely identified as such are excluded from both the numerator and the denominator for purposes of the 95% gross income test (but are non-qualifying income for purposes of the 75% gross income test). Income and gain from hedging transactions to hedge indebtedness incurred or to be incurred to acquire or carry real estate assets and that are clearly and timely identified as such entered into after July 30, 2008 are excluded from both the numerator and the denominator for purposes of both the 75% and 95% gross income tests. In addition, certain foreign currency gains recognized after July 30, 2008 will be excluded from gross income for purposes of one or both of the gross income tests. See “—Foreign Currency Gain.” We will monitor the amount of our nonqualifying income and we will manage our portfolio to comply at all times with the gross income tests. The following paragraphs discuss the specific application of the gross income tests to us.

Interest. The term “interest,” as defined for purposes of both gross income tests, generally excludes any amount that is based in whole or in part on the income or profits of any person. However, interest generally includes the following:

- an amount that is based on a fixed percentage or percentages of receipts or sales; and
- an amount that is based on the income or profits of a debtor, as long as the debtor derives substantially all of its income from the real property securing the debt from leasing substantially all of its interest in the property, and only to the extent that the amounts received by the debtor would be qualifying “rents from real property” if received

directly by a REIT.

- 14 -

If a loan contains a provision that entitles a REIT to a percentage of the borrower's gain upon the sale of the real property securing the loan or a percentage of the appreciation in the property's value as of a specific date, income attributable to that loan provision will be treated as gain from the sale of the property securing the loan, which generally is qualifying income for purposes of both gross income tests.

Interest on debt secured by a mortgage on real property or on interests in real property, including, for this purpose, discount points, prepayment penalties, loan assumption fees, and late payment charges that are not compensation for services, generally is qualifying income for purposes of the 75% gross income test. However, if the highest principal amount of a loan outstanding during a taxable year exceeds the fair market value of the real property securing the loan as of the date the REIT agreed to originate or acquire the loan and the loan is secured by property other than real property, a portion of the interest income from such loan will not be qualifying income for purposes of the 75% gross income test, but will be qualifying income for purposes of the 95% gross income test. The portion of the interest income that will not be qualifying income for purposes of the 75% gross income test will be equal to the portion of the principal amount of the loan that is not secured by real property — that is, the amount by which the loan exceeds the value of the real estate that is security for the loan.

We primarily own Agency residential mortgage-backed securities ("MBS"). Other than income from imbedded derivative instruments as described below, all of the income on our Agency MBS is qualifying income for purposes of the 95% gross income test. The Agency MBS are treated either as interests in a grantor trust or as interests in a REMIC for federal income tax purposes. In the case of Agency MBS treated as interests in grantor trusts, such as our whole-pool pass-through securities, we are treated as owning an undivided beneficial ownership interest in the mortgage loans held by the grantor trust. The interest on such mortgage loans is qualifying income for purposes of the 75% gross income test to the extent that the obligation is secured by real property, as discussed above. In the case of Agency MBS treated as interests in a REMIC, such as our CMOs, IOs, POs and IIOs, income derived from REMIC interests will generally be treated as qualifying income for purposes of the 75% gross income test. If less than 95% of the assets of the REMIC are real estate assets, however, then only a proportionate part of our interest in the REMIC and income derived from the interest will qualify for purposes of the 95% gross income test. In addition, some REMIC securitizations include imbedded interest swap or cap contracts or other derivative instruments that potentially could produce non-qualifying income for the holders of the related REMIC securities. We believe that substantially all of our income from Agency MBS is qualifying income for the 75% and 95% gross income tests.

The interest, original issue discount, and market discount income that we receive from our Agency MBS generally will be qualifying income for purposes of both gross income tests. However, as discussed above, if the fair market value of the real estate securing any of our loans is less than the principal amount of the loan, a portion of the income from that loan will be qualifying income for purposes of the 95% gross income test but not the 75% gross income test.

Dividends. Our share of any dividends received from any corporation (including any TRS, but excluding any REIT) in which we own an equity interest will qualify for purposes of the 95% gross income test but not for purposes of the 75% gross income test. Our share of any dividends received from any other REIT in which we own an equity interest will be qualifying income for purposes of both gross income tests.

Fee Income. Fee income generally is qualifying income for purposes of both the 75% and 95% gross income tests if it is received in consideration for entering into an agreement to make a loan secured by real property and the fees are not determined by income and profits. Other fees generally are not qualifying income for purposes of either gross income test. Any fees earned by a TRS are not included for purposes of the gross income tests.

Foreign Currency Gain. Certain foreign currency gains recognized after July 30, 2008 are excluded from gross income for purposes of one or both of the gross income tests. “Real estate foreign exchange gain” is excluded from gross income for purposes of the 75% gross income test. Real estate foreign exchange gain generally includes foreign currency gain attributable to any item of income or gain that is qualifying income for purposes of the 75% gross income test, foreign currency gain attributable to the acquisition or ownership of (or becoming or being the obligor under) obligations secured by mortgages on real property or on interest in real property and certain foreign currency gain attributable to certain “qualified business units” of a REIT. “Passive foreign exchange gain” is excluded from gross income for purposes of the 95% gross income test. Passive foreign exchange gain generally includes real estate foreign exchange gain as described above, and also includes foreign currency gain attributable to any item of income or gain that is qualifying income for purposes of the 95% gross income test and foreign currency gain attributable to the acquisition or ownership of (or becoming or being the obligor under) debt obligations. Because passive foreign exchange gain includes real estate foreign exchange gain, real estate foreign exchange gain is excluded from gross income for purposes of both the 75% and 95% gross income test. These exclusions for real estate foreign exchange gain and passive foreign exchange gain do not apply to foreign currency gain derived from dealing, or engaging in substantial and regular trading, in securities. Such gain is treated as non-qualifying income for purposes of both the 75% and 95% gross income tests.

Rents from Real Property. Except for the real property that we own for use in the operation of our business, we do not hold and do not intend to acquire any real property. However, we may acquire real property or an interest therein in the future. To the extent that we acquire real property or an interest therein, rents we receive will qualify as “rents from real property” in satisfying the gross income requirements for a REIT described above only if the following conditions are met:

- First, the amount of rent must not be based in whole or in part on the income or profits of any person. However, an amount received or accrued generally will not be excluded from rents from real property solely by reason of being based on fixed percentages of receipts or sales.
- Second, rents we receive from a “related party tenant” will not qualify as rents from real property in satisfying the gross income tests unless the tenant is a TRS, at least 90% of the property is leased to unrelated tenants and the rent paid by the TRS is substantially comparable to the rent paid by the unrelated tenants for comparable space and the rent is not attributable to a modification of a lease with a controlled TRS (i.e., a TRS in which we own directly or indirectly more than 50% of the voting power or value of the stock). A tenant is a related party tenant if the REIT, or an actual or constructive owner of 10% or more of the REIT, actually or constructively owns 10% or more of the tenant.
- Third, if rent attributable to personal property, leased in connection with a lease of real property, is greater than 15% of the total rent received under the lease, then the portion of rent attributable to the personal property will not qualify as rents from real property.
- Fourth, we generally must not operate or manage our real property or furnish or render noncustomary services to our tenants, other than through an “independent contractor” who is adequately compensated and from whom we do not derive revenue. However, we may provide services directly to tenants if the services are “usually or customarily rendered” in connection with the rental of space for occupancy only and are not considered to be provided for the tenants’ convenience. In addition, we may provide a minimal amount of “noncustomary” services to the tenants of a property, other than through an independent contractor, as long as our income from the services does not exceed 1% of our income from the related property. Furthermore, we may own up to 100% of the stock of a TRS, which may provide customary and noncustomary services to tenants without tainting its rental income from the related properties.

Hedging Transactions. From time to time, we enter into hedging transactions with respect to one or more of our assets or liabilities. Our hedging activities may include entering into interest rate swaps, caps, and floors, options to purchase these items, and futures and forward contracts. Income and gain from “hedging transactions” entered into on or before July 30, 2008 is excluded from gross income for purposes of the 95% gross income test (but is treated as nonqualifying income for purposes of the 75% gross income test). Income and gain from hedging transactions entered into after July 30, 2008 are excluded from gross income for purposes of both the 75% and 95% gross income tests. A “hedging transaction” includes any transaction entered into in the normal course of our trade or business primarily to manage the risk of interest rate changes, price changes, or currency fluctuations with respect to borrowings made or to be made, or ordinary obligations incurred or to be incurred, to acquire or carry real estate assets. A “hedging transaction” also includes any transaction entered into after July 30, 2008 primarily to manage risk of currency fluctuations with respect to any item of income or gain that is qualifying income for purposes of the 75% or 95% gross income test (or any property which generates such income or gain). We are required to clearly identify any such hedging transaction before the close of the day on which it was acquired, originated, or entered into and satisfy other identification requirements. To the extent that we hedge or for other purposes, the income from those transactions is not likely to be treated as qualifying income for purposes of the gross income tests. We have structured and intend to continue to structure any hedging transactions in a manner that does not jeopardize our status as a REIT.

Prohibited Transactions. A REIT incurs a 100% tax on the net income (including foreign currency gain recognized after July 30, 2008) derived from any sale or other disposition of property, other than foreclosure property, that the REIT holds primarily for sale to customers in the ordinary course of a trade or business. We believe that none of our assets will be held primarily for sale to customers and that a sale of any of our assets will not be in the ordinary course of our business. Whether a REIT holds an asset “primarily for sale to customers in the ordinary course of a trade or business” depends, however, on the facts and circumstances in effect from time to time, including those related to a particular asset. Nevertheless, we will attempt to comply with the terms of safe-harbor provisions in the federal income tax laws prescribing when an asset sale will not be characterized as a prohibited transaction. We cannot assure you, however, that we can comply with the safe-harbor provisions or that we will avoid owning property that may be characterized as property that we hold “primarily for sale to customers in the ordinary course of a trade or business.”

Foreclosure Property. We are subject to tax at the maximum corporate rate on any income (including foreign currency gain recognized after July 30, 2008) from foreclosure property, other than income that otherwise would be qualifying income for purposes of the 75% gross income test, less expenses directly connected with the production of that income. However, gross income from foreclosure property will qualify under the 75% and 95% gross income tests. Foreclosure property is any real property, including interests in real property, and any personal property incident to such real property:

- that is acquired by a REIT as the result of the REIT having bid on such property at foreclosure, or having otherwise reduced such property to ownership or possession by agreement or process of law, after there was a default or default was imminent on a lease of such property or on indebtedness that such property secured;
- for which the related loan or lease was acquired by the REIT at a time when the default was not imminent or anticipated; and
 - for which the REIT makes a proper election to treat the property as foreclosure property.

However, a REIT will not be considered to have foreclosed on a property where the REIT takes control of the property as a mortgagee-in-possession and cannot receive any profit or sustain any loss except as a creditor of the mortgagor. Property generally ceases to be foreclosure property at the end of the third taxable year following the taxable year in which the REIT acquired the property, or longer if an extension is granted by the Secretary of the Treasury. This grace period terminates and foreclosure property ceases to be foreclosure property on the first day:

- on which a lease is entered into for the property that, by its terms, will give rise to income that does not qualify for purposes of the 75% gross income test, or any amount is received or accrued, directly or indirectly, pursuant to a lease entered into on or after such day that will give rise to income that does not qualify for purposes of the 75% gross income test;

- 17 -

- on which any construction takes place on the property, other than completion of a building or any other improvement, where more than 10% of the construction was completed before default became imminent; or
- which is more than 90 days after the day on which the REIT acquired the property and the property is used in a trade or business which is conducted by the REIT, other than through an independent contractor from whom the REIT itself does not derive or receive any income.

Failure to Satisfy Gross Income Tests. If we fail to satisfy one or both of the gross income tests for any taxable year, we nevertheless may qualify as a REIT for that year if we qualify for relief under certain provisions of the federal income tax laws. Those relief provisions generally will be available if:

- our failure to meet such tests was due to reasonable cause and not due to willful neglect; and
- following such failure for any taxable year, a schedule of the sources of our income is filed with the IRS.

We cannot predict, however, whether in all circumstances we would qualify for the relief provisions. In addition, as discussed above in “— Taxation of Our Company,” even if the relief provisions apply, we would incur a 100% tax on the gross income attributable to the greater of (i) the amount by which we fail the 75% gross income test or (ii) the amount by which 95% of our gross income exceeds the amount of our income qualifying under the 95% gross income test, multiplied by a fraction intended to reflect our profitability.

Asset Tests

To qualify as a REIT, we also must satisfy the following asset tests at the end of each quarter of each taxable year. First, at least 75% of the value of our total assets must consist of:

- cash or cash items, including certain receivables;
 - government securities;
- interests in real property, including leaseholds and options to acquire real property and leaseholds;
 - interests in mortgage loans secured by real property;
 - stock in other REITs;
- investments in stock or debt instruments during the one-year period following our receipt of new capital that we raise through equity offerings or public offerings of debt with at least a five-year term; and
- regular or residual interests in a REMIC. However, if less than 95% of the assets of a REMIC consist of assets that are qualifying real estate-related assets under the federal income tax laws, determined as if we held such assets, we will be treated as holding directly our proportionate share of the assets of such REMIC.

Second, of our investments not included in the 75% asset class, the value of our interest in any one issuer’s securities may not exceed 5% of the value of our total assets.

Third, of our investments not included in the 75% asset class, we may not own more than 10% of the voting power or value of any one issuer's outstanding securities.

- 18 -

Fourth, no more than 25% (20% for taxable years prior to 2009) of the value of our total assets may consist of the securities of one or more TRSs.

Fifth, no more than 25% of the value of our total assets may consist of the securities of TRSs and other non-TRS taxable subsidiaries and other assets that are not qualifying assets for purposes of the 75% asset test.

For purposes of the second and third asset tests, the term “securities” does not include stock in another REIT, equity or debt securities of a qualified REIT subsidiary or TRS, mortgage loans that constitute real estate assets, or equity interests in a partnership. For purposes of the 10% value test, the term “securities” does not include:

- “Straight debt” securities, which is defined as a written unconditional promise to pay on demand or on a specified date a sum certain in money if (i) the debt is not convertible, directly or indirectly, into stock, and (ii) the interest rate and interest payment dates are not contingent on profits, the borrower’s discretion, or similar factors. “Straight debt” securities do not include any securities issued by a partnership or a corporation in which we or any controlled TRS (i.e., a TRS in which we own directly or indirectly more than 50% of the voting power or value of the stock) hold non-“straight debt” securities that have an aggregate value of more than 1% of the issuer’s outstanding securities. However, “straight debt” securities include debt subject to the following contingencies:
 - a contingency relating to the time of payment of interest or principal, as long as either (i) there is no change to the effective yield of the debt obligation, other than a change to the annual yield that does not exceed the greater of 0.25% or 5% of the annual yield, or (ii) neither the aggregate issue price nor the aggregate face amount of the issuer’s debt obligations held by us exceeds \$1 million and no more than 12 months of unaccrued interest on the debt obligations can be required to be prepaid; and
 - a contingency relating to the time or amount of payment upon a default or prepayment of a debt obligation, as long as the contingency is consistent with customary commercial practice.
 - Any loan to an individual or an estate.
 - Any “section 467 rental agreement,” other than an agreement with a related party tenant.
 - Any obligation to pay “rents from real property.”
 - Certain securities issued by governmental entities.
 - Any security issued by a REIT.
- Any debt instrument of an entity treated as a partnership for federal income tax purposes to the extent of our interest as a partner in the partnership.
- Any debt instrument of an entity treated as a partnership for federal income tax purposes not described in the preceding bullet points if at least 75% of the partnership’s gross income, excluding income from prohibited transactions, is qualifying income for purposes of the 75% gross income test described above in “—Requirements for Qualification — Gross Income Tests.”

The asset tests described above are based on our gross assets. We believe that our Agency MBS qualify as real estate assets or as government securities.

We enter into sale and repurchase agreements under which we nominally sell certain of our Agency MBS to a counterparty and simultaneously enter into an agreement to repurchase the sold assets in exchange for a purchase price that reflects a financing charge. Based on positions the IRS has taken in analogous situations, we believe that we are treated for REIT asset and income test purposes as the owner of the Agency MBS that are the subject of such agreements notwithstanding that such agreements may transfer record ownership of the assets to the counterparty during the term of the agreement. It is possible, however, that the IRS could assert that we did not own the Agency MBS during the term of the sale and repurchase agreement, in which case we could fail to qualify as a REIT.

We will monitor the status of our assets for purposes of the various asset tests and will seek to manage our portfolio to comply at all times with such tests. There can be no assurance, however, that we will be successful in this effort. In this regard, to determine our compliance with these requirements, we will need to value our investment in our assets to ensure compliance with the asset tests. Although we will seek to be prudent in making these estimates, there can be no assurances that the IRS might not disagree with these determinations and assert that a lower value is applicable. If we fail to satisfy the asset tests at the end of a calendar quarter, we will not lose our REIT status if:

- we satisfied the asset tests at the end of the preceding calendar quarter; and
- the discrepancy between the value of our assets and the asset test requirements arose from changes in the market values of our assets and was not wholly or partly caused by the acquisition of one or more non-qualifying assets.

If we did not satisfy the condition described in the second item above, we still could avoid disqualification by eliminating any discrepancy within 30 days after the close of the calendar quarter in which it arose.

In the event that, at the end of any calendar quarter, we violate the second or third asset tests described above, we will not lose our REIT status if (i) the failure is de minimis (up to the lesser of 1% of our assets or \$10 million) and (ii) we dispose of assets or otherwise comply with the asset tests within six months after the last day of the quarter in which we identify such failure. In the event of a more than de minimis failure of any of the asset tests, as long as the failure was due to reasonable cause and not to willful neglect, we will not lose our REIT status if we (i) dispose of assets or otherwise comply with the asset tests within six months after the last day of the quarter in which we identify such failure, (ii) file a description of the assets that caused such failure with the IRS, and (iii) pay a tax equal to the greater of \$50,000 or 35% of the net income from the nonqualifying assets during the period in which we failed to satisfy the asset tests.

We currently believe that our assets satisfy the foregoing asset test requirements. However, no independent appraisals have been or will be obtained to support our conclusions as to the value of our assets and securities, or in many cases, the real estate collateral for the mortgage loans that support our Agency MBS. Moreover, the values of some assets may not be susceptible to a precise determination. As a result, there can be no assurance that the IRS will not contend that our ownership of securities and other assets violates one or more of the asset tests applicable to REITs.

Distribution Requirements

Each taxable year we must distribute dividends, other than capital gain dividends and deemed distributions of retained capital gain, to our stockholders in an aggregate amount at least equal to:

- the sum of
 - 90% of our “REIT taxable income,” computed without regard to the dividends paid deduction and our net capital gain or loss, and

- 90% of our after-tax net income, if any, from foreclosure property, minus

- the sum of certain items of non-cash income.

We must pay such distributions in the taxable year to which they relate, or in the following taxable year if we declare the distribution before we timely file our federal income tax return for the year and pay the distribution on or before the first regular dividend payment date after such declaration.

In order for distributions to be counted as satisfying the annual distribution requirements for REITs, and to provide us with a REIT-level tax deduction, the distributions must not be “preferential dividends.” A dividend is not a preferential dividend if the distribution is (1) pro-rata among all outstanding shares of stock within a particular class, and (2) in accordance with the preferences among different classes of stock as set forth in our organizational documents.

We will pay federal income tax on taxable income, including net capital gain, which we do not distribute to stockholders. Furthermore, if we fail to distribute during a calendar year, or by the end of January of the following calendar year in the case of distributions with declaration and record dates falling in the last three months of the calendar year, at least the sum of:

- 85% of our REIT ordinary income for such year,
- 95% of our REIT capital gain income for such year, and
- any undistributed taxable income from prior periods,

We will incur a 4% nondeductible excise tax on the excess of such required distribution over the amounts we actually distribute. We may elect to retain and pay income tax on the net long-term capital gain we receive in a taxable year. If we so elect, we will be treated as having distributed any such retained amount for purposes of the 4% nondeductible excise tax described above. We intend to continue to make timely distributions sufficient to satisfy the annual distribution requirements and to avoid corporate income tax and the 4% nondeductible excise tax.

It is possible that, from time to time, we may experience timing differences between the actual receipt of income and actual payment of deductible expenses and the inclusion of that income and deduction of such expenses in arriving at our REIT taxable income. Possible examples of those timing differences include the following:

- Because we may deduct capital losses only to the extent of our capital gains, we may have taxable income that exceeds our economic income.
- We will recognize taxable income in advance of the related cash flow if any of our MBS are deemed to have original issue discount. We generally must accrue original issue discount based on a constant yield method that takes into account projected prepayments but that defers taking into account credit losses until they are actually incurred.
- We may recognize taxable market discount income when we receive the proceeds from the disposition of, or principal payments on, loans that have a stated redemption price at maturity that is greater than our tax basis in those loans, although such proceeds often will be used to make non-deductible principal payments on related borrowings.
-

We may recognize taxable income without receiving a corresponding cash distribution if we foreclose on or make a significant modification to a loan, to the extent that the fair market value of the underlying property or the principal amount of the modified loan, as applicable, exceeds our basis in the original loan.

- We may recognize taxable income from any residual interests in REMICs or retained ownership interests in mortgage loans subject to collateralized mortgage obligation debt.

Although several types of non-cash income are excluded in determining the annual distribution requirement, we will incur corporate income tax and the 4% nondeductible excise tax with respect to those non-cash income items if we do not distribute those items on a current basis. As a result of the foregoing, we may have less cash than is necessary to distribute all of our taxable income and thereby avoid corporate income tax and the excise tax imposed on certain undistributed income. In such a situation, we may need to borrow funds or issue additional common or preferred stock.

Under certain circumstances, we may be able to correct a failure to meet the distribution requirement for a year by paying “deficiency dividends” to our stockholders in a later year. We may include such deficiency dividends in our deduction for dividends paid for the earlier year. Although we may be able to avoid income tax on amounts distributed as deficiency dividends, we will be required to pay interest to the IRS based upon the amount of any deduction we take for deficiency dividends.

Recordkeeping Requirements

We must maintain certain records in order to qualify as a REIT. In addition, to avoid a monetary penalty, we must annually request information from our stockholders designed to disclose the actual ownership of our outstanding stock. We believe we fully comply with these requirements.

Failure to Qualify

If we fail to satisfy one or more requirements for REIT qualification, other than the gross income tests and the asset tests, we could avoid disqualification if our failure is due to reasonable cause and not to willful neglect and we pay a penalty of \$50,000 for each such failure. In addition, there are relief provisions for a failure of the gross income tests and asset tests, as described in “— Requirements for Qualification — Gross Income Tests” and “— Requirements for Qualification — Asset Tests.”

If we fail to qualify as a REIT in any taxable year, and no relief provision applies, we would be subject to federal income tax and any applicable alternative minimum tax on our taxable income at regular corporate rates. In calculating our taxable income in a year in which we fail to qualify as a REIT, we would not be able to deduct amounts paid out to stockholders. In fact, we would not be required to distribute any amounts to stockholders in that year. In such event, to the extent of our current and accumulated earnings and profits, all distributions to stockholders would be taxable as ordinary income. Subject to certain limitations of the federal income tax laws, corporate stockholders might be eligible for the dividends received deduction and domestic non-corporate stockholders might be eligible for the reduced federal income tax rate of 15% on such dividends. Unless we qualified for relief under specific statutory provisions, we also would be disqualified from taxation as a REIT for the four taxable years following the year during which we ceased to qualify as a REIT. We cannot predict whether in all circumstances we would qualify for such statutory relief.

Taxation of Taxable U.S. Stockholders

The term “U.S. stockholder” means a holder of our common stock that, for United States federal income tax purposes, is:

- a citizen or resident of the United States;

- a corporation or partnership (including an entity treated as a corporation or partnership for U.S. federal income tax purposes) created or organized under the laws of the United States, any of its states or the District of Columbia;
 - an estate whose income is subject to federal income taxation regardless of its source; or
- any trust if (i) a U.S. court is able to exercise primary supervision over the administration of such trust and one or more U.S. persons have the authority to control all substantial decisions of the trust or (ii) it has a valid election in place to be treated as a U.S. person.

As long as we qualify as a REIT, a taxable “U.S. stockholder” must take into account as ordinary income distributions made out of our current or accumulated earnings and profits that we do not designate as capital gain dividends or retained long-term capital gain. A U.S. stockholder will not qualify for the dividends received deduction generally available to corporations. In addition, dividends paid by a REIT to a U.S. stockholder generally will not qualify for the 15% tax rate for “qualified dividend income.” Qualified dividend income generally includes dividends paid by domestic C corporations and certain qualified foreign corporations to most U.S. noncorporate stockholders. Because we are not generally subject to federal income tax on the portion of our REIT taxable income distributed to our stockholders, our dividends generally will not be eligible for the new 15% rate on qualified dividend income. As a result, our ordinary REIT dividends will continue to be taxed at the higher tax rate applicable to ordinary income. Currently, the highest marginal individual income tax rate on ordinary income is 35%. However, the 15% tax rate for qualified dividend income will apply to our ordinary REIT dividends, if any, that are (i) attributable to dividends received by us from non-REIT corporations, such as our TRSs, and (ii) attributable to income upon which we have paid corporate income tax (e.g., to the extent that we distribute less than 100% of our taxable income). In general, to qualify for the reduced tax rate on qualified dividend income, a stockholder must hold our common stock for more than 60 days during the 121-day period beginning on the date that is 60 days before the date on which our stock becomes ex-dividend.

If we declare a distribution in October, November, or December of any year that is payable to a U.S. stockholder of record on a specified date in any such month, such distribution shall be treated as both paid by us and received by the U.S. stockholder on December 31 of such year, provided that we actually pay the distribution during January of the following calendar year. These dividends are referred to as “January dividends.”

A U.S. stockholder generally will recognize distributions that we designate as capital gain dividends as long-term capital gain without regard to the period for which the U.S. stockholder has held its common stock. We generally will designate our capital gain dividends as either 15% or 25% rate distributions. See “—Capital Gains and Losses.” A corporate U.S. stockholder, however, may be required to treat up to 20% of certain capital gain dividends as a preference item.

We may elect to retain and pay income tax on the net long-term capital gain that we recognize in a taxable year. In that case, a U.S. stockholder would be taxed on its proportionate share of our undistributed long-term capital gain. The U.S. stockholder would receive a credit or refund for its proportionate share of the tax we paid. The U.S. stockholder would increase the basis in its common stock by the amount of its proportionate share of our undistributed long-term capital gain, minus its share of the tax we paid.

A U.S. stockholder will not incur tax on a distribution in excess of our current and accumulated earnings and profits if the distribution does not exceed the adjusted basis of the U.S. stockholder’s common stock. Instead, the distribution will reduce the adjusted basis of such common stock. A U.S. stockholder will recognize a distribution in excess of both our current and accumulated earnings and profits and the U.S. stockholder’s adjusted basis in his or her common stock as long-term capital gain, or short-term capital gain if the common stock has been held for one year or less, assuming the common stock is a capital asset in the hands of the U.S. stockholder.

Stockholders may not include in their individual income tax returns any of our net operating losses or capital losses; instead, these losses are generally carried over by us for potential offset against our future REIT taxable income or realized capital gains, respectively. Taxable distributions from us and gain from the disposition of the common stock will not be treated as passive activity income and, therefore, stockholders generally will not be able to apply any “passive activity losses,” such as losses from certain types of limited partnerships in which the stockholder is a limited partner, against such income. In addition, taxable distributions from us and gain from the disposition of our common stock generally will be treated as investment income for purposes of the investment interest limitations. We will notify stockholders after the close of our taxable year as to the portions of the distributions attributable to that year that constitute ordinary income, return of capital, and capital gain.

Our excess inclusion income generally will be allocated among our stockholders to the extent that it exceeds our REIT taxable income in a particular year. A stockholder's share of excess inclusion income would not be allowed to be offset by any net operating losses otherwise available to the stockholder.

- 23 -

Taxation of U.S. Stockholders on the Disposition of Common Stock

In general, a U.S. stockholder who is not a dealer in securities must treat any gain or loss realized upon a taxable disposition of our common stock as long-term capital gain or loss if the U.S. stockholder has held the common stock for more than one year and otherwise as short-term capital gain or loss. However, a U.S. stockholder must treat any loss upon a sale or exchange of common stock held by such stockholder for six-months or less as a long-term capital loss to the extent of capital gain dividends and any other actual or deemed distributions from us that such U.S. stockholder treats as long-term capital gain. All or a portion of any loss that a U.S. stockholder realizes upon a taxable disposition of the common stock may be disallowed if the U.S. stockholder purchases substantially identical common stock within 30 days before or after the disposition.

Capital Gains and Losses

A taxpayer generally must hold a capital asset for more than one year for gain or loss derived from its sale or exchange to be treated as long-term capital gain or loss. The highest marginal individual income tax rate currently is 35%. The maximum tax rate on long-term capital gain applicable to non-corporate taxpayers is currently 15%. The maximum tax rate on long-term capital gain from the sale or exchange of “section 1250 property,” or depreciable real property, is 25% to the extent that such gain would have been treated as ordinary income if the property were “section 1245 property.” With respect to distributions that we designate as capital gain dividends and any retained capital gain that we are deemed to distribute, we generally may designate whether such a distribution is taxable to our non-corporate stockholders at a 15% or 25% rate. Thus, the tax rate differential between capital gain and ordinary income for non-corporate taxpayers may be significant. In addition, the characterization of income as capital gain or ordinary income may affect the deductibility of capital losses. A non-corporate taxpayer may deduct capital losses not offset by capital gains against its ordinary income only up to a maximum annual amount of \$3,000 (\$1,500 for married individuals filing separate returns). A non-corporate taxpayer may carry forward unused capital losses indefinitely. A corporate taxpayer must pay tax on its net capital gain at ordinary corporate rates. A corporate taxpayer may deduct capital losses only to the extent of capital gains, with unused losses being carried back three years and forward five years.

Taxation of Tax-Exempt Stockholders

Tax-exempt entities, including qualified employee pension and profit sharing trusts and individual retirement accounts and annuities, generally are exempt from federal income taxation. However, they are subject to taxation on their unrelated business taxable income. While many investments in real estate generate unrelated business taxable income, the IRS has issued a published ruling that dividend distributions from a REIT to an exempt employee pension trust do not constitute unrelated business taxable income, provided that the exempt employee pension trust does not otherwise use the shares of the REIT in an unrelated trade or business of the pension trust. Based on that ruling, amounts that we distribute to tax-exempt stockholders generally should not constitute unrelated business taxable income. However, if a tax-exempt stockholder were to finance its investment in our common stock with debt, a portion of the income that it receives from us would constitute unrelated business taxable income pursuant to the “debt-financed property” rules. In addition, our dividends that are attributable to excess inclusion income will constitute unrelated business taxable income in the hands of most tax-exempt stockholders. Furthermore, social clubs, voluntary employee benefit associations, supplemental unemployment benefit trusts, and qualified group legal services plans that are exempt from taxation under special provisions of the federal income tax laws are subject to different unrelated business taxable income rules, which generally will require them to characterize distributions that they receive from us as unrelated business taxable income. Finally, in certain circumstances, a qualified employee pension or profit sharing trust that owns more than 10% of our stock is required to treat a percentage of the dividends that it receives from us as unrelated business taxable income. Such percentage is equal to the gross income that we derive from an unrelated trade or business, determined as if we were a pension trust, divided by our total gross income for the year in which we pay the dividends. That rule applies to a pension trust holding more than 10% of our stock only if:

- the percentage of our dividends that the tax-exempt trust would be required to treat as unrelated business taxable income is at least 5%;
- we qualify as a REIT by reason of the modification of the rule requiring that no more than 50% of our stock be owned by five or fewer individuals that allows the beneficiaries of the pension trust to be treated as holding our stock in proportion to their actuarial interests in the pension trust; and
- either: (i) one pension trust owns more than 25% of the value of our stock or (ii) a group of pension trusts individually holding more than 10% of the value of our stock collectively owns more than 50% of the value of our stock.

Taxation of Non-U.S. Stockholders

The term “non-U.S. stockholder” means a holder of our common stock that is not a U.S. stockholder or a partnership (or entity treated as a partnership for federal income tax purposes). The rules governing federal income taxation of nonresident alien individuals, foreign corporations, foreign partnerships, and other non-U.S. stockholders are complex. This section is only a general summary of such rules. We urge non-U.S. stockholders to consult their own tax advisors to determine the impact of federal, foreign, state, and local income tax laws on ownership of our stock, including any reporting requirements.

A non-U.S. stockholder that receives a distribution that is not attributable to gain from our sale or exchange of U.S. real property interests, as defined below, and that we do not designate as a capital gain dividend or retained capital gain will recognize ordinary income to the extent that we pay the distribution out of our current or accumulated earnings and profits. A withholding tax equal to 30% of the gross amount of the distribution ordinarily will apply unless an applicable tax treaty reduces or eliminates the tax. However, if a distribution is treated as effectively connected with the non-U.S. stockholder’s conduct of a U.S. trade or business, the non-U.S. stockholder generally will be subject to federal income tax on the distribution at graduated rates, in the same manner as U.S. stockholders are taxed on distributions and also may be subject to the 30% branch profits tax in the case of a corporate non-U.S. stockholder. We plan to withhold U.S. income tax at the rate of 30% on the gross amount of any ordinary dividend paid to a non-U.S. stockholder unless either:

- a lower treaty rate applies and the non-U.S. stockholder files an IRS Form W-8BEN evidencing eligibility for that reduced rate with us, or
- the non-U.S. stockholder files an IRS Form W-8ECI with us claiming that the distribution is effectively connected income.

However, reduced treaty rates are not available to the extent that the income allocated to the foreign stockholder is excess inclusion income. Our excess inclusion income generally will be allocated among our stockholders to the extent that it exceeds our REIT taxable income in a particular year.

A non-U.S. stockholder will not incur U.S. tax on a distribution in excess of our current and accumulated earnings and profits if the excess portion of the distribution does not exceed the adjusted basis of its common stock. Instead, the excess portion of the distribution will reduce the adjusted basis of that common stock. A non-U.S. stockholder will be subject to tax on a distribution that exceeds both our current and accumulated earnings and profits and the adjusted basis of the common stock, if the non-U.S. stockholder otherwise would be subject to tax on gain from the sale or disposition of its common stock, as described below. Because we generally cannot determine at the time we make a distribution whether or not the distribution will exceed our current and accumulated earnings and profits, we normally

will withhold tax on the entire amount of any distribution at the same rate as we would withhold on a dividend. However, by filing a U.S. tax return, a non-U.S. stockholder may obtain a refund of amounts that we withhold if we later determine that a distribution in fact exceeded our current and accumulated earnings and profits.

- 25 -

For any year in which we qualify as a REIT, a non-U.S. stockholder could incur tax on distributions that are attributable to gain from our sale or exchange of “United States real property interests” under special provisions of the federal income tax laws known as the Foreign Investment in Real Property Tax Act of 1980 (“FIRPTA”). The term “United States real property interests” includes interests in real property and shares in corporations at least 50% of whose assets consist of interests in real property. We do not expect to make significant distributions that are attributable to gain from our sale or exchange of U.S. real property interests. Moreover, any distributions that are attributable to our sale of real property will not be subject to FIRPTA, but instead will be treated as ordinary dividends as long as (1) our shares of common stock are “regularly traded” on an established securities market in the United States and (2) the non-U.S. stockholder did not own more than 5% of the class of our stock on which the distribution is made during the one-year period ending on the date of the distribution. If, however, we were to make a distribution that is attributable to gain from our sale or exchange of U.S. real property interests and a non-U.S. stockholder were subject to FIRPTA on that distribution, the non-U.S. stockholder would be taxed on the distribution as if such amount were effectively connected with a U.S. business of the non-U.S. Holder. A non-U.S. stockholder thus would be taxed on such a distribution at the normal capital gains rates applicable to U.S. stockholders, subject to applicable alternative minimum tax and a special alternative minimum tax in the case of a nonresident alien individual. A non-U.S. corporate stockholder not entitled to treaty relief or exemption also could be subject to the 30% branch profits tax on such a distribution. We must withhold 35% of any distribution that we could designate as a capital gain dividend. A non-U.S. stockholder would receive a credit against its U.S. federal income tax liability for any amount we withhold.

A non-U.S. stockholder should not incur a tax under FIRPTA on gains from the disposition of our common stock because we are not and do not expect to be a U.S. real property holding corporation, or a corporation the fair market value of whose U.S. real property interests equals or exceeds 50% of the fair market value of its stock. In addition, even if we were to become a U.S. real property holding corporation, a non-U.S. stockholder would not incur tax under FIRPTA with respect to gain realized upon a disposition of our common stock as long as at all times non-U.S. persons hold, directly or indirectly, less than 50% in value of our outstanding stock. Moreover, even if we are treated as a U.S. real property holding corporation, a non-U.S. stockholder that owned, actually or constructively, 5% or less of our common stock at all times during a specified testing period would not incur tax under FIRPTA on gain from the disposition of our common stock if the class of stock held is “regularly traded” on an established securities market. However, a non-U.S. stockholder generally will incur tax on gain not subject to FIRPTA if:

- the gain is effectively connected with the non-U.S. stockholder’s U.S. trade or business, in which case the non-U.S. stockholder will be subject to the same treatment as U.S. stockholders with respect to such gain, or
- the non-U.S. stockholder is a nonresident alien individual who was present in the U.S. for 183 days or more during the taxable year and has a “tax home” in the United States, in which case the non-U.S. stockholder will incur a tax of 30% on his or her capital gains.

Information Reporting Requirements and Backup Withholding

We will report to our stockholders and to the IRS the amount of dividends we pay during each calendar year, whether those dividends are taxable or return-of-capital, and the amount of tax we withhold, if any. Under the backup withholding rules, a stockholder may be subject to backup withholding at a rate of 28% with respect to distributions unless the holder:

- is a corporation or comes within certain other exempt categories and, when required, demonstrates this fact; or
- provides a taxpayer identification number, certifies as to no loss of exemption from backup withholding, and otherwise complies with the applicable requirements of the backup withholding rules.

A stockholder who does not provide us with its correct taxpayer identification number also may be subject to penalties imposed by the IRS. Any amount paid as backup withholding will be creditable against the stockholder's income tax liability. In addition, we may be required to withhold a portion of capital gain distributions to any stockholders who fail to certify their non-foreign status to us.

- 26 -

Backup withholding will generally not apply to payments of dividends made by us or our paying agents, in their capacities as such, to a non-U.S. stockholder provided that the non-U.S. stockholder furnishes to us or our paying agent the required certification as to its non-U.S. status, such as providing a valid IRS Form W-8BEN or W-8ECI, or certain other requirements are met. Notwithstanding the foregoing, backup withholding may apply if either we or our paying agent has actual knowledge, or reason to know, that the holder is a U.S. person that is not an exempt recipient. Payments of the net proceeds from a disposition or a redemption effected outside the U.S. by a non-U.S. stockholder made by or through a foreign office of a broker generally will not be subject to information reporting or backup withholding. However, information reporting (but not backup withholding) generally will apply to such a payment if the broker has certain connections with the U.S. unless the broker has documentary evidence in its records that the beneficial owner is a non-U.S. stockholder and specified conditions are met or an exemption is otherwise established. Payment of the net proceeds from a disposition by a non-U.S. stockholder of common shares made by or through the U.S. office of a broker is generally subject to information reporting and backup withholding unless the non-U.S. stockholder certifies under penalties of perjury that it is not a U.S. person and satisfies certain other requirements, or otherwise establishes an exemption from information reporting and backup withholding.

Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules may be refunded or credited against the shareholder's federal income tax liability if certain required information is furnished to the IRS. Stockholders are urged to consult their own tax advisors regarding application of backup withholding to them and the availability of, and procedure for obtaining an exemption from, backup withholding.

Taxable REIT Subsidiaries

As described above, we may own up to 100% of the stock of one or more TRSs. We presently have two TRS subsidiaries, both of which are 100% owned by Bimini Capital. A TRS is a fully taxable corporation that may earn income that would not be qualifying income if earned directly by a REIT. A corporation will not qualify as a TRS if it directly or indirectly operates or manages any hotels or health care facilities or provides rights to any brand name under which any hotel or health care facility is operated, except to the extent such facility is managed by an "eligible independent contractor" on behalf of the TRS.

We must make an election for each subsidiary to be treated as a TRS. A corporation of which a qualifying TRS directly or indirectly owns more than 35% of the voting power or value of the stock will automatically be treated as a TRS. Overall, no more than 25% of the value of our assets may consist of securities of one or more TRSs, and no more than 25% of the value of our assets may consist of the securities of TRSs and other non-TRS taxable subsidiaries and other assets that are not qualifying assets for purposes of the 75% asset test.

The TRS rules limit the deductibility of interest paid or accrued by a TRS to us to assure that the TRS is subject to an appropriate level of corporate taxation. Further, the rules impose a 100% excise tax on transactions between a TRS and us or our tenants that are not conducted on an arm's-length basis.

We have elected to treat MortCo and Bimini Advisors as TRSs. MortCo and Bimini Advisors are subject to corporate income tax on their own taxable income. We believe that all transactions between Bimini Capital and both of our TRSs have been and will be conducted on an arm's-length basis.

Potential Limitation on Use of Net Operating Losses

As of December 31, 2011, MortCo had a federal net operating loss (“NOL”) carryforwards of approximately \$270.8 million, which will be available to offset future taxable income of MortCo, subject to the limitations described below. No assurance can be provided that MortCo will have future taxable income to benefit from its NOL carryforwards. In addition, MortCo’s ability to use its NOL carryforwards may be limited by Section 382 of the Code, if MortCo undergoes an “ownership change” as defined in that section. Generally, there is an “ownership change” if, at any time, one or more 5.0% stockholders (as defined in the Code) have aggregate increases in their ownership of the corporation of more than 50 percentage points looking back over the relevant testing period, which can occur as a result of direct and indirect acquisitions and certain dispositions of stock by the corporation’s 5.0% stockholders. Because MortCo is wholly owned by us, these definitions are generally applied at the REIT level. If an “ownership change” occurs, MortCo’s ability to use its NOL carryforwards to reduce its taxable income in a future year would generally be limited to an annual amount, or the “Section 382 Limitation,” equal to the fair value of MortCo immediately prior to the Ownership Change multiplied by an interest rate specified by the IRS in published revenue rulings. In the event of an “ownership change,” NOL carryforwards that exceed the Section 382 Limitation in any year will continue to be allowed as carryforwards for the remainder of the carryforward period, and such NOL carryforwards can be used to offset taxable income for years within the carryforward period subject to the Section 382 Limitation in each year. However, if the carryforward period for any NOL carryforwards were to expire before that loss was fully utilized, the unused portion of that loss would be lost. At December 31, 2011, Bimini Advisors’ NOL was not material.

Our Board of Directors has set the general ownership limit applicable to our Class A Common stock at 4.98%. The Board of Directors, in its sole discretion, may allow certain shareholders to own up to a 9.8% limit. This ownership limit is intended, in part, to preserve the benefit of the MortCo’s NOL carryforwards for tax purposes, as well as any NOL carryforwards at the REIT level. However, there is no guarantee that MortCo will not experience an “ownership change,” in which case its ability to offset its taxable income with its NOL carryforwards will be significantly limited.

Sunset of Reduced Tax Rate Provisions

Several of the tax considerations described herein are subject to a sunset provision in the Code as it is presently written. Based on tax laws enacted in December 2010, the sunset provisions generally provide that, for taxable years beginning after December 31, 2012, certain provisions that are currently in the Code will revert back to a prior version of those provisions. These provisions include provisions related to the reduced maximum income tax rate for long term capital gains of 15% (rather than 20%) for taxpayers taxed at individual rates, the application of the 15% tax rate to qualified dividend income, and certain other tax rate provisions described herein. The impact of this reversion is not discussed herein. Consequently, you should consult your tax advisor regarding the effect of sunset provisions on an investment in our common stock.

State, Local and Foreign Taxes

We and/or our stockholders may be subject to taxation by various states, localities or foreign jurisdictions, including those in which we or a stockholder transacts business, owns property or resides. We may own properties located in numerous jurisdictions and may be required to file tax returns in some or all of those jurisdictions. The state, local and foreign tax treatment may differ from the federal income tax treatment described above. Consequently, you should consult your tax advisor regarding the effect of state, local and foreign income and other tax laws upon an investment

in the common stock.

- 28 -

COMPETITION

We operate in the mortgage-REIT industry. We believe that our principal competition in the acquisition and holding of the types of mortgage-backed securities we purchase are financial institutions such as banks, savings and loans, life insurance companies, institutional investors such as mutual funds and pension funds, and certain other mortgage REITs. Many of our competitors have greater financial resources and access to capital than we do and may not be subject to the same regulatory constraints (i.e., REIT compliance or maintaining an exemption under the Investment Company Act) as us. Our competitors, as well as additional competitors which may emerge in the future, may increase the competition for the acquisition of mortgage-backed securities, which in turn may result in higher prices and lower yields on assets.

AVAILABLE INFORMATION

We are subject to the reporting requirements of the Securities Act of 1934 (“Exchange Act”), as amended, and its rules and regulations. The Exchange Act requires us to file reports, proxy statements, and other information with the Securities and Exchange Commission (“SEC”). Copies of these reports, proxy statements, and other information can be read and copied at the SEC’s Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549, on official business days during the hours of 10 a.m. to 3 p.m. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains a website that contains reports, proxy statements, and other information regarding issuers that file electronically with the SEC. These materials may be obtained electronically by accessing the SEC’s home page at <http://www.sec.gov>.

Our website can be found at www.biminicapital.com. Our annual reports on Form 10-K, our quarterly reports on Form 10-Q and our current reports on Form 8-K, and amendments to those reports, filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act, are made available free of charge through our website as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC.

ITEM 1A. RISK FACTORS.

RISKS RELATED TO OUR BUSINESS

Continued adverse developments in the broader residential mortgage market have adversely affected Bimini and may materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

The residential mortgage market in the United States has experienced a variety of difficulties and changed economic conditions, including defaults, credit losses and liquidity concerns. In addition, certain commercial banks, investment banks and insurance companies have announced extensive losses from exposure to the residential mortgage market. These losses have reduced financial industry capital, leading to reduced liquidity for some institutions. These factors have impacted investor perception of the risk associated with real estate-related assets, including Agency MBS. As a result, values for MBS, including some Agency MBS and other AAA-rated MBS assets, have been negatively impacted. Further increased volatility and deterioration in the broader residential mortgage and MBS markets may adversely affect the performance and market value of the Agency MBS in which we invest.

We rely on our Agency MBS as collateral for our financings. Any decline in their value, or perceived market uncertainty about their value, would likely make it difficult for us to obtain financing on favorable terms or at all or maintain our compliance with terms of any financing arrangements already in place. Additionally, the Company has elected to account for its investment in MBS under the fair value option and, therefore, will be reported on our financial statements at fair value with unrealized gains and losses included in earnings. If market conditions result in a

decline in the value of our Agency MBS, our business, financial position and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

- 29 -

In 2005, Bimini Capital acquired MortCo, an originator of residential mortgage loans. At the time MortCo was acquired, Bimini managed an Agency MBS portfolio with a fair value of approximately \$3.5 billion. MortCo operated in 46 states and originated residential mortgages through three production channels. MortCo did not have the capacity to retain the mortgages it originated, and relied on the ability to sell loans as they were originated as either whole loans or through off-balance sheet securitizations. When the residential housing market in the United States started to collapse in late 2006 and early 2007, the ability to execute this strategy was quickly impaired as whole loan prices plummeted and the securitization markets closed. Bimini's management closed a majority of the mortgage origination operations in early 2007, with the balance sold by June 30, 2007. Additional losses were incurred after June 30, 2007 as the remaining assets were sold or became impaired, and by December 31, 2009, MortCo had an accumulated deficit of approximately \$278 million. The losses generated by MortCo required Bimini to slowly liquidate its Agency MBS portfolio as capital was reduced and the operations of MortCo drained cash resources. On November 5, 2007, Bimini was delisted by the NYSE. By December 31, 2008, Bimini's Agency MBS portfolio was reduced to approximately \$172 million and, as a result of the reduced capital remaining and the financial crisis, Bimini had limited access to repurchase agreement funding.

We have issued long-term debt to fund our operations which can increase the volatility of our earnings and stockholders' equity.

In October 2005, Bimini Capital completed a private offering of trust preferred securities of Bimini Capital Trust II, of which \$26.8 million are still outstanding. The Company must pay interest on these junior subordinated notes on a quarterly basis at a rate equal to current three month LIBOR rate plus 3.5%. To the extent the Company's does not generate sufficient earnings to cover the interest payments on the debt, our earnings and stockholders' equity may be negatively impacted.

The Company considers the junior subordinated notes as part of its long-term capital base. Therefore, for purposes of all disclosure in this report concerning our capital or leverage, the Company considers both stockholders' equity and the \$26.8 million of junior subordinated notes to constitute capital.

The Company has also elected to account for its investments in MBS under the fair value option and, therefore, will report MBS on our financial statements at fair value with unrealized gains and losses included in earnings. Changes in the value of the MBS do not impact the outstanding balance of the junior subordinated notes but rather our stockholders' equity. Therefore, changes in the value of our MBS will be absorbed solely by our stockholders' equity. Because our stockholders equity is small in relation to our total capital, such changes may result in significant changes in our stockholders' equity.

Interest rate mismatches between our Agency MBS and our borrowings may reduce our net interest margin during periods of changing interest rates, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our portfolio includes Agency MBS backed by ARMs, hybrid ARMs and fixed-rate mortgages, and the mix of these securities in the portfolio may be increased or decreased over time. Additionally, the interest rates on ARMs and hybrid ARMs may vary over time based on changes in a short-term interest rate index, of which there are many.

We finance our acquisitions of pass-through Agency MBS with short-term financing. During periods of rising short-term interest rates, the income we earn on these securities will not change (with respect to Agency MBS backed by fixed-rate mortgage loans) or will not increase at the same rate (with respect to Agency MBS backed by ARMs and hybrid ARMs) as our related financing costs, which may reduce our net interest margin or result in losses.

The federal conservatorship of Fannie Mae and Freddie Mac and related efforts, along with any changes in laws and regulations affecting the relationship between Fannie Mae and Freddie Mac and the U.S. Government, may adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

The payments we receive on the Agency MBS in which we invest depend upon a steady stream of payments on the mortgages underlying the securities and are guaranteed by Ginnie Mae, Fannie Mae or Freddie Mac. Ginnie Mae is part of a U.S. Government agency and its guarantees are backed by the full faith and credit of the United States. Fannie Mae and Freddie Mac are U.S. Government sponsored entities, or GSEs, but their guarantees are not backed by the full faith and credit of the United States.

Since 2007, Fannie Mae and Freddie Mac have reported substantial losses and a need for substantial amounts of additional capital. In response to the deteriorating financial condition of Fannie Mae and Freddie Mac and the recent credit market disruption, Congress and the US Treasury have undertaken a series of actions to stabilize these GSEs and the financial markets generally. The Housing and Economic Recovery Act was signed into law on July 30, 2008, and it established the Federal Housing Finance Authority, or FHFA. On September 7, 2008, the FHFA placed Fannie Mae and Freddie Mac into conservatorship, which is a statutory process pursuant to which the FHFA operates Fannie Mae and Freddie Mac in an effort to stabilize the entities. The FHFA, together with the U.S. Treasury and the U.S. Federal Reserve, has also undertaken actions designed to boost investor confidence in Fannie Mae and Freddie Mac, support the availability of mortgage financing and protect taxpayers. In addition, the U.S. Treasury has taken steps to capitalize and provide financing to Fannie Mae and Freddie Mac and agreed to purchase direct obligations and Agency MBS issued or guaranteed by Fannie Mae or Freddie Mac.

Shortly after Fannie Mae and Freddie Mac were placed in federal conservatorship, the Secretary of the U.S. Treasury, in announcing the actions, noted that the guarantee structure of Fannie Mae and Freddie Mac required examination and that changes in the structures of the entities were necessary to reduce risk to the financial system. In February 2011, the U.S. Treasury and the Department of Housing and Urban Development released a White Paper titled "Reforming America's Housing Finance Market," or the Housing Report, in which they propose reducing or eliminating the role of GSEs in mortgage financing. The Housing Report calls for phasing in increased pricing of Fannie Mae and Freddie Mac guarantees to help level the playing field for the private sector to take back market share, reducing conforming loan limits by allowing the temporary increase in Fannie Mae's and Freddie Mac's conforming loan limits to reset as scheduled on October 1, 2011 to the lower levels set in the Housing and Economic Recovery Act of 2008 and continuing to wind down Fannie Mae's and Freddie Mac's investment portfolio at an annual rate of no less than 10% per year. The future roles of Fannie Mae and Freddie Mac could be significantly reduced and the nature of their guarantees could be eliminated or considerably limited relative to historical measurements. Any changes to the nature of the guarantees provided by Fannie Mae and Freddie Mac could redefine what constitutes Agency MBS, have broad adverse market implications and negatively impact us.

The problems faced by Fannie Mae and Freddie Mac resulting in their being placed into Federal conservatorship have stirred debate among some federal policy makers regarding the continued role of the U.S. Government in providing liquidity for the residential mortgage market. If federal policy makers decide that the U.S. Government's role in providing liquidity for the residential mortgage market should be reduced or eliminated, each of Fannie Mae and Freddie Mac could be dissolved and the U.S. Government could decide to stop providing liquidity support of any kind to the mortgage market. If Fannie Mae or Freddie Mac were eliminated, or their structures were to change radically, we may not be able to acquire Agency MBS from these companies, which could drastically reduce the amount and type of Agency MBS available for investment, thereby increasing the price of these assets. Additionally, the current credit support provided by the U.S. Treasury to Fannie Mae and Freddie Mac, and any additional credit support it may provide in the future, could have the effect of lowering the interest rate we receive from Agency MBS, thereby tightening the spread between the interest we earn on our portfolio and our financing costs. Additionally, the U.S. Government could elect to stop providing credit support of any kind to the mortgage market. If any of these events

were to occur, our business, financial condition and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

- 31 -

As indicated above, recent legislation has changed the relationship between Fannie Mae and Freddie Mac and the U.S. Government and requires Fannie Mae and Freddie Mac to reduce the amount of mortgage loans they own or the amount of Agency MBS for which they provide guarantees. The effect of the actions taken by the U.S. Government remains uncertain. Furthermore, the scope and nature of the actions that the U.S. Government will ultimately undertake are unknown and will continue to evolve. Future legislation could further change the relationship between Fannie Mae and Freddie Mac and the U.S. Government and could also nationalize or eliminate these GSEs entirely. Any law affecting these GSEs may create market uncertainty and have the effect of reducing the actual or perceived credit quality of securities issued or guaranteed by Fannie Mae or Freddie Mac. As a result, such laws could adversely impact the market for such securities and the spreads at which they trade. All of the foregoing could materially adversely affect the pricing, supply, liquidity and value of our target assets and otherwise materially adversely affect our business, financial condition, and results of operations and our ability to pay distributions to our stockholders.

Certain actions by the U.S. Federal Reserve could cause a flattening of the yield curve, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

On September 21, 2011, the U.S. Federal Reserve announced “Operation Twist,” a program pursuant to which it intends to purchase \$400 billion of U.S. Treasury securities with remaining maturities between six and 30 years and sell an equal amount of such securities with remaining maturities of three years or less by the end of June 2012. The effect of Operation Twist could be a flattening of the yield curve, which could result in increased prepayment rates due to lower long-term interest rates and a narrowing of our net interest margin. Consequently, Operation Twist and any other future securities purchase programs of the U.S. Federal Reserve could materially adversely affect our business, financial condition, and results of operations and our ability to pay distributions to our stockholders.

Mortgage loan modification programs and future legislative action may adversely affect the value of, and the returns on, our Agency MBS, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

During the second half of 2008, the U.S. Government commenced programs designed to provide homeowners with assistance in avoiding residential mortgage loan foreclosures. The programs involve, among other things, the modification of mortgage loans to reduce the principal amount of the loans or the rate of interest payable on the loans, or to extend the payment terms of the loans.

In addition, in February 2008, the U.S. Treasury announced the Homeowner Affordability and Stability Plan, or HASP, which is a multi-faceted plan intended to prevent residential mortgage foreclosures by, among other things:

- allowing certain homeowners whose homes are encumbered by Fannie Mae or Freddie Mac conforming mortgages to refinance those mortgages into lower interest rate mortgages with either Fannie Mae or Freddie Mac;
- creating the Homeowner Stability Initiative, which is intended to utilize various incentives for banks and mortgage servicers to modify residential mortgage loans with the goal of reducing monthly mortgage principal and interest payments for certain qualified homeowners; and
- allowing judicial modifications of Fannie Mae and Freddie Mac conforming residential mortgages loans during bankruptcy proceedings.

In September 2011, the White House announced that they are working on a major plan to allow some of the 11 million homeowners who owe more on their mortgages than their homes are worth to refinance. In October 2011, the FHFA announced proposed changes to the Home Affordable Refinance Program, or HARP, that would expand access to refinancing for qualified individuals and families whose homes have lost value by, among other things, increasing the HARP loan-to-value ratio above 125%. However, this would only apply to mortgages guaranteed by the GSEs. There are many challenging issues to this proposal, notably the question as to whether a loan with a loan-to-value ratio of 125% qualifies as a mortgage or an unsecured consumer loan. The chances of this initiative's success have created additional uncertainty in the MBS market, particularly with respect to possible increases in prepayment rates.

On January 4, 2012, the U.S. Federal Reserve issued a white paper outlining additional ideas with regard to refinancings and loan modifications. It is likely that loan modifications would result in increased prepayments on some Agency MBS. See “—Prepayment rates could negatively affect the value of our Agency MBS, which could result in reduced earnings or losses and negatively affect the cash available for distribution to our stockholders,” for more information relating to the impact of prepayment on our business. These initiatives, any future loan modification programs and future legislative or regulatory actions, including amendments to the bankruptcy laws, that result in the modification of outstanding mortgage loans may adversely affect the value of, and the returns on, the Agency MBS in which we invest.

The downgrade of the U.S.'s and certain European countries' credit ratings and any future downgrades of the U.S.'s and certain European countries' credit ratings may materially adversely affect our business, financial condition and results of operations.

On August 5, 2011, Standard & Poor's downgraded the U.S.'s credit rating for the first time in history. Because Fannie Mae and Freddie Mac are in conservatorship of the U.S. Government, downgrades to the U.S.'s credit rating could impact the credit risk associated with Agency MBS and, therefore, decrease the value of the Agency MBS in our portfolio. In addition, the downgrade of the U.S. Government's credit rating and the credit ratings of certain European countries has created broader financial turmoil and uncertainty, which has weighed heavily on the global banking system. Therefore, the recent downgrade of the U.S.'s credit rating and the credit ratings of certain European countries and any future downgrades of the U.S.'s credit rating and the credit ratings of certain European countries may materially adversely affect our business, financial condition and results of operations.

Prepayment rates could negatively affect the value of our Agency MBS, which could result in reduced earnings or losses and negatively affect the cash available for distribution to our stockholders.

In the case of residential mortgage loans, there are seldom any restrictions on borrowers' abilities to prepay their loans. Homeowners tend to prepay mortgage loans faster when applicable mortgage interest rates decline. Furthermore, both HARP and Operation Twist could cause an increase in prepayment rates. Consequently, owners of the loans have to reinvest the money received from the prepayments at the lower prevailing interest rates. Conversely, homeowners tend not to prepay mortgage loans when mortgage interest rates remain steady or increase. Consequently, owners of the loans are unable to reinvest money that would have otherwise been received from prepayments at the higher prevailing interest rates. This volatility in prepayment rates may affect our ability to maintain targeted amounts of leverage on our Agency MBS portfolio, result in reduced earnings or losses for us and negatively affect the cash available for distribution to our stockholders.

Fannie Mae, Freddie Mac or Ginnie Mae guarantees of principal and interest related to the Agency MBS we own do not protect us against prepayment risks.

We invest in structured Agency MBS, including CMOs, IOs, IIOs and POs. Although structured Agency MBS are generally subject to the same risks as our PT MBS, certain types of risks may be enhanced depending on the type of structured Agency MBS in which we invest.

The structured Agency MBS in which we invest are securitizations (i) issued by Fannie Mae, Freddie Mac or Ginnie Mae, (ii) collateralized by Agency MBS and (iii) divided into various tranches that have different characteristics (such as different maturities or different coupon payments). These securities may carry greater risk than an investment in PT MBS. For example, certain types of structured Agency MBS, such as IOs, IIOs and POs, are more sensitive to prepayment risks than PT MBS. If we were to invest in structured Agency MBS that were more sensitive to prepayment risks relative to other types of structured Agency MBS or pass-through Agency MBS, we may increase our portfolio-wide prepayment risk.

Increased levels of prepayments on the mortgages underlying our Agency MBS might decrease net interest income or result in a net loss, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

In the case of residential mortgages, there are seldom any restrictions on borrowers' ability to prepay their loans. Prepayment rates generally increase when interest rates fall and decrease when interest rates rise. Prepayment rates also may be affected by other factors, including, without limitation, conditions in the housing and financial markets, governmental action (such as HARP and Operation Twist), general economic conditions and the relative interest rates on ARMs, hybrid ARMs and fixed-rate mortgage loans. With respect to pass-through Agency MBS, faster-than-expected prepayments could also materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders in various ways, including the following:

- A portion of our pass-through Agency MBS backed by ARMs and hybrid ARMs may initially bear interest at rates that are lower than their fully indexed rates, which are equivalent to the applicable index rate plus a margin. If a PT MBS backed by ARMs or hybrid ARMs is prepaid prior to or soon after the time of adjustment to a fully-indexed rate, we will have held that Agency MBS while it was less profitable and lost the opportunity to receive interest at the fully-indexed rate over the remainder of its expected life.
- If we are unable to acquire new Agency MBS to replace the prepaid Agency MBS, our returns on capital may be lower than if we were able to quickly acquire new Agency MBS.

When we acquire structured Agency MBS, we anticipate that the underlying mortgages will prepay at a projected rate, generating an expected yield. When the prepayment rates on the mortgages underlying our structured Agency MBS are higher than expected, our returns on those securities may be materially adversely affected. For example, the value of our IOs and IIOs are extremely sensitive to prepayments because holders of these securities do not have the right to receive any principal payments on the underlying mortgages. Therefore, if the mortgage loans underlying our IOs and IIOs are prepaid, such securities would cease to have any value, which, in turn, could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

While we seek to minimize prepayment risk, we must balance prepayment risk against other risks and the potential returns of each investment. No strategy can completely insulate us from prepayment or other such risks.

A decrease in prepayment rates on the mortgages underlying our Agency MBS might decrease net interest income or result in a net loss, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Certain of our structured Agency MBS may be adversely affected by a decrease in prepayment rates. For example, because POs are similar to zero-coupon bonds, our expected returns on such securities will be contingent on our receiving the principal payments of the underlying mortgage loans at expected intervals that assume a certain prepayment rate. If prepayment rates are lower than expected, we will not receive principal payments as quickly as we anticipated and, therefore, our expected returns on these securities will be adversely affected, which, in turn, could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

The U.S. Government's pressing for refinancing of certain loans may affect prepayment rates for mortgage loans underlying our Agency MBS.

In addition to the increased pressure upon residential mortgage loan investors and servicers to engage in loss mitigation activities, the U.S. Government is pressing for refinancing of certain loans, and this encouragement may affect prepayment rates for mortgage loans underlying our Agency MBS. To the extent these and other economic stabilization or stimulus efforts are successful in increasing prepayment speeds for residential mortgage loans, such as those in Agency MBS, our income and operating results could be harmed, particularly in connection with our IOs and IIOs, which, in turn, could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Interest rate caps on the ARMs and hybrid ARMs backing our Agency MBS may reduce our net interest margin during periods of rising interest rates, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

ARMs and hybrid ARMs are typically subject to periodic and lifetime interest rate caps. Periodic interest rate caps limit the amount an interest rate can increase during any given period. Lifetime interest rate caps limit the amount an interest rate can increase through the maturity of the loan. Our borrowings typically are not subject to similar restrictions. Accordingly, in a period of rapidly increasing interest rates, our financing costs could increase without limitation while caps could limit the interest we earn on the ARMs and hybrid ARMs backing our Agency MBS. This problem is magnified for ARMs and hybrid ARMs that are not fully indexed because such periodic interest rate caps prevent the coupon on the security from fully reaching the specified rate in one reset. Further, some ARMs and hybrid ARMs may be subject to periodic payment caps that result in a portion of the interest being deferred and added to the principal outstanding. As a result, we may receive less cash income on Agency MBS backed by ARMs and hybrid ARMs than necessary to pay interest on our related borrowings. Interest rate caps on Agency MBS backed by ARMs and hybrid ARMs could reduce our net interest margin if interest rates were to increase beyond the level of the caps, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We rely on analytical models and other data to analyze potential asset acquisition and disposition opportunities and to manage our portfolio. Such models and other data may be incorrect, misleading or incomplete, which could cause us to purchase assets that do not meet our expectations or to make asset management decisions that are not in line with our strategy.

We rely on analytical models and other data supplied by third parties. These models and data may be used to value assets or potential asset acquisitions and dispositions and also in connection with our asset management activities. If our models and data prove to be incorrect, misleading or incomplete, any decisions made in reliance thereon could

expose us to potential risks.

Our reliance on models and data may induce us to purchase certain assets at prices that are too high, to sell certain other assets at prices that are too low or to miss favorable opportunities altogether. Similarly, any hedging activities that are based on faulty models and data may prove to be unsuccessful.

- 35 -

Some models, such as prepayment models, may be predictive in nature. The use of predictive models has inherent risks. For example, such models may incorrectly forecast future behavior, leading to potential losses. In addition, the predictive models used by us may differ substantially from those models used by other market participants, resulting in valuations based on these predictive models that may be substantially higher or lower for certain assets than actual market prices. Furthermore, because predictive models are usually constructed based on historical data supplied by third parties, the success of relying on such models may depend heavily on the accuracy and reliability of the supplied historical data, and, in the case of predicting performance in scenarios with little or no historical precedent (such as extreme broad-based declines in home prices, or deep economic recessions or depressions), such models must employ greater degrees of extrapolation and are therefore more speculative and less reliable.

All valuation models rely on correct market data input. If incorrect market data is entered into even a well-founded valuation model, the resulting valuations will be incorrect. However, even if market data is inputted correctly, “model prices” will often differ substantially from market prices, especially for securities with complex characteristics or whose values are particularly sensitive to various factors. If our market data inputs are incorrect or our model prices differ substantially from market prices, our business, financial condition and results of operations and our ability to make distributions to our stockholders could be materially adversely affected.

Valuations of some of our assets are inherently uncertain, may be based on estimates, may fluctuate over short periods of time and may differ from the values that would have been used if a ready market for these assets existed. As a result, the values of some of our assets are uncertain.

While in many cases our determination of the fair value of our assets is based on valuations provided by third-party dealers and pricing services, we can and do value assets based upon our judgment, and such valuations may differ from those provided by third-party dealers and pricing services. Valuations of certain assets are often difficult to obtain or are unreliable. In general, dealers and pricing services heavily disclaim their valuations. Additionally, dealers may claim to furnish valuations only as an accommodation and without special compensation, and so they may disclaim any and all liability for any direct, incidental or consequential damages arising out of any inaccuracy or incompleteness in valuations, including any act of negligence or breach of any warranty. Depending on the complexity and illiquidity of an asset, valuations of the same asset can vary substantially from one dealer or pricing service to another. The valuation process has been particularly difficult recently because market events have made valuations of certain assets more difficult and unpredictable and the disparity of valuations provided by third-party dealers has widened.

Our business, financial condition and results of operations and our ability to make distributions to our stockholders could be materially adversely affected if our fair value determinations of these assets were materially higher than the values that would exist if a ready market existed for these assets.

An increase in interest rates may cause a decrease in the volume of newly issued, or investor demand for, Agency MBS, which could materially adversely affect our ability to acquire assets that satisfy our investment objectives and our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Rising interest rates generally reduce the demand for consumer credit, including mortgage loans, due to the higher cost of borrowing. A reduction in the volume of mortgage loans may affect the volume of Agency MBS available to us, which could affect our ability to acquire assets that satisfy our investment objectives. Rising interest rates may also result in Agency MBS that were issued prior to an interest rate increase having yields that do not exceed prevailing market interest rates. If rising interest rates cause us to be unable to acquire a sufficient volume of Agency MBS or Agency MBS with a yield that exceeds our borrowing costs, our ability to satisfy our investment objectives and to generate income and pay dividends, our business, financial condition and results of operations and our ability to pay distributions to our stockholders may be materially adversely affected.

Because the assets that we acquire might experience periods of illiquidity, we might be prevented from selling our Agency MBS at favorable times and prices, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Agency MBS generally experience periods of illiquidity. Such conditions are more likely to occur for structured Agency MBS because such securities are generally traded in markets much less liquid than the pass-through Agency MBS market. As a result, we may be unable to dispose of our Agency MBS at advantageous times and prices or in a timely manner. The lack of liquidity might result from the absence of a willing buyer or an established market for these assets as well as legal or contractual restrictions on resale. The illiquidity of Agency MBS could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our use of leverage could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Under normal market conditions, we generally expect our leverage ratio to be less than 12 to 1, although at times our borrowings may be above or below this level. We incur this indebtedness by borrowing against a substantial portion of the market value of our pass-through Agency MBS and a portion of our structured Agency MBS. Our total indebtedness, however, is not expressly limited by our policies and will depend on our and our prospective lenders' estimates of the stability of our portfolio's cash flow. As a result, there is no limit on the amount of leverage that we may incur. We face the risk that we might not be able to meet our debt service obligations or a lender's margin requirements from our income and, to the extent we cannot, we might be forced to liquidate some of our Agency MBS at unfavorable prices. Our use of leverage could materially adversely affect our business, financial condition and results of operation and our ability to pay distributions to our stockholders. For example:

- Our repurchase agreement borrowings are secured by our pass-through Agency MBS and may be secured by a portion of our structured Agency MBS under repurchase agreements. A decline in the market value of the pass-through Agency MBS or structured Agency MBS used to secure these debt obligations could limit our ability to borrow or result in lenders requiring us to pledge additional collateral to secure our borrowings. In that situation, we could be required to sell Agency MBS under adverse market conditions in order to obtain the additional collateral required by the lender. If these sales are made at prices lower than the carrying value of the Agency MBS, we would experience losses.
- To the extent we are compelled to liquidate qualifying real estate assets to repay debts, our compliance with the REIT rules regarding our assets and our sources of gross income could be negatively affected, which could jeopardize our qualification as a REIT. Losing our REIT qualification would cause us to be subject to U.S. federal income tax (and any applicable state and local taxes) on all of our income and would decrease profitability and cash available for distributions to stockholders.

If we experience losses as a result of our use of leverage, such losses could materially adversely affect our business, results of operations and financial condition and our ability to make distributions to our stockholders.

We may incur increased borrowing costs, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our borrowing costs under repurchase agreements are generally adjustable and correspond to short-term interest rates, such as LIBOR or a short-term U.S. Treasury index, plus or minus a margin. The margins on these borrowings over or under short-term interest rates may vary depending upon a number of factors, including, without limitation:

- the movement of interest rates;

- the availability of financing in the market; and
- the value and liquidity of our Agency MBS.

All of our short-term borrowings are collateralized borrowings in the form of repurchase agreements. If the interest rates on these repurchase agreements increase, our business, financial condition and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

Failure to procure adequate repurchase agreement financing, or to renew or replace existing repurchase agreement financing as it matures, could materially adversely affect our business, financial condition and results of operations and our ability to make distributions to our stockholders.

We currently have master repurchase agreements with five counterparties. We cannot provide assurance that any, or sufficient, repurchase agreement financing will be available to us in the future on terms that are acceptable to us. Any decline in the value of Agency MBS, or perceived market uncertainty about their value, would make it more difficult for us to obtain financing on favorable terms or at all, or maintain our compliance with the terms of any financing arrangements already in place. Additionally, our lenders may have owned or financed MBS that have declined in value and caused the lender to suffer losses as a result of the recent downturn in the residential mortgage market. If these conditions persist, these institutions may be forced to exit the repurchase market, become insolvent or further tighten lending standards or increase the amount of equity capital, or haircuts, required to obtain financing, and in such event, could make it more difficult for us to obtain financing on favorable terms or at all. Additionally, we may be unable to diversify the credit risk associated with our lenders. In the event that we cannot obtain sufficient funding on acceptable terms, our business, financial condition and results of operations and our ability to pay distributions to our stockholders may be materially adversely effected.

Furthermore, because we intend to rely primarily on short-term borrowings to fund our MBS, our ability to achieve our investment objective will depend not only on our ability to borrow money in sufficient amounts and on favorable terms, but also on our ability to renew or replace on a continuous basis our maturing short-term borrowings. If we are not able to renew or replace maturing borrowings, we will have to sell some or all of our assets, possibly under adverse market conditions. In addition, if the regulatory capital requirements imposed on our lenders change, they may be required to significantly increase the cost of the financing that they provide to us. Our lenders also may revise their eligibility requirements for the types of assets they are willing to finance or the terms of such financings, based on, among other factors, the regulatory environment and their management of perceived risk.

Adverse market developments could cause our lenders to require us to pledge additional assets as collateral. If our assets were insufficient to meet these collateral requirements, we might be compelled to liquidate particular assets at inopportune times and at unfavorable prices, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Adverse market developments, including a sharp or prolonged rise in interest rates, a change in prepayment rates or increasing market concern about the value or liquidity of one or more types of Agency MBS, might reduce the market value of our portfolio, which might cause our lenders to initiate margin calls. A margin call means that the lender requires us to pledge additional collateral to re-establish the ratio of the value of the collateral to the amount of the borrowing. The specific collateral value to borrowing ratio that would trigger a margin call is not set in the master repurchase agreements and not determined until we engage in a repurchase transaction under these agreements. Our fixed-rate Agency MBS generally are more susceptible to margin calls as increases in interest rates tend to more negatively affect the market value of fixed-rate securities. If we are unable to satisfy margin calls, our lenders may foreclose on our collateral. The threat or occurrence of a margin call could force us to sell either directly or through a foreclosure our Agency MBS under adverse market conditions. Because of the significant leverage we expect to have, we may incur substantial losses upon the threat or occurrence of a margin call, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders. Additionally, the liquidation of collateral may jeopardize our ability to qualify or maintain our qualification as a REIT, as we must comply with requirements regarding our assets and our sources of gross income. If we are compelled to liquidate our Agency MBS, we may be unable to comply with these requirements, ultimately jeopardizing our ability to qualify or maintain our qualification as a REIT. Our failure to qualify as a REIT or maintain our qualification would cause us to be subject to U.S. federal income tax (and any applicable state and local taxes) on all of our income.

Our use of repurchase agreements may give our lenders greater rights in the event that either we or any of our lenders file for bankruptcy, which may make it difficult for us to recover our collateral in the event of a bankruptcy filing.

Our borrowings under repurchase agreements may qualify for special treatment under the bankruptcy code, giving our lenders the ability to avoid the automatic stay provisions of the bankruptcy code and to take possession of and liquidate our collateral under the repurchase agreements without delay if we file for bankruptcy. Furthermore, the special treatment of repurchase agreements under the bankruptcy code may make it difficult for us to recover our pledged assets in the event that any of our lenders files for bankruptcy. Thus, the use of repurchase agreements exposes our pledged assets to risk in the event of a bankruptcy filing by either our lenders or us. In addition, if the lender is a broker or dealer subject to the Securities Investor Protection Act of 1970, or an insured depository institution subject to the Federal Deposit Insurance Act, our ability to exercise our rights to recover our investment under a repurchase agreement or to be compensated for any damages resulting from the lender's insolvency may be further limited by those statutes.

On October 31, 2011, MF Global, one of our former repurchase agreement counterparties, filed for Chapter 11 bankruptcy. At the time of MF Global's bankruptcy filing, we did not have any repurchase agreements in place with MF Global, however, MF Global held approximately \$0.3 million of cash related to repurchase agreements in place prior to their bankruptcy filing. To date, we have not recovered this cash, and MF Global is no longer one of our repurchase agreement counterparties. We cannot assure you that we will recover all or any of the remaining collateral cash in the future.

If we fail to maintain our relationship with AVM, L.P. or if we do not establish relationships with other repurchase agreement trading, clearing and administrative service providers, our business, financial condition and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

We have engaged AVM, L.P. to provide us with certain repurchase agreement trading, clearing and administrative services. If we are unable to maintain our relationship with AVM, L.P. or we are unable to establish successful relationships with other repurchase agreement trading, clearing and administrative service providers, our business, financial condition and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

- 39 -

If our lenders default on their obligations to resell the Agency MBS back to us at the end of the repurchase transaction term, or if the value of the Agency MBS has declined by the end of the repurchase transaction term or if we default on our obligations under the repurchase transaction, we will lose money on these transactions, which, in turn, may materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

When we engage in a repurchase transaction, we initially sell securities to the financial institution under one of our master repurchase agreements in exchange for cash, and our counterparty is obligated to resell the securities to us at the end of the term of the transaction, which is typically from 24 to 90 days but may be up to 364 days or more. The cash we receive when we initially sell the securities is less than the value of those securities, which is referred to as the haircut. Many financial institutions from which we may obtain repurchase agreement financing have increased their haircuts in the past and may do so again in the future. As of December 31, 2011, our haircuts were approximately 5% on average, which means that we will be required to pledge Agency MBS the value of which equals approximately 105% of the principal amount of the borrowings. If these haircuts are increased, we will be required to post additional cash or securities as collateral for our Agency MBS. If our counterparty defaults on its obligation to resell the securities to us, we would incur a loss on the transaction equal to the amount of the haircut (assuming there was no change in the value of the securities). We would also lose money on a repurchase transaction if the value of the underlying securities had declined as of the end of the transaction term, as we would have to repurchase the securities for their initial value but would receive securities worth less than that amount. Any losses we incur on our repurchase transactions could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

If we default on one of our obligations under a repurchase transaction, the counterparty can terminate the transaction and cease entering into any other repurchase transactions with us. In that case, we would likely need to establish a replacement repurchase facility with another financial institution in order to continue to leverage our portfolio and carry out our investment strategy. There is no assurance we would be able to establish a suitable replacement facility on acceptable terms or at all.

Hedging against interest rate exposure may not completely insulate us from interest rate risk and could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

To the extent consistent with qualifying and maintaining our qualification as a REIT, we may enter into interest rate cap or swap agreements or pursue other hedging strategies, including the purchase of puts, calls or other options and futures contracts in order to hedge the interest rate risk of our portfolio. In general, our hedging strategy depends on our view of our entire portfolio consisting of assets, liabilities and derivative instruments, in light of prevailing market conditions. We could misjudge the condition of our investment portfolio or the market. Our hedging activity will vary in scope based on the level and volatility of interest rates and principal prepayments, the type of Agency MBS we hold and other changing market conditions. Hedging may fail to protect or could adversely affect us because, among other things:

- hedging can be expensive, particularly during periods of rising and volatile interest rates;
- available interest rate hedging may not correspond directly with the interest rate risk for which protection is sought;
 - the duration of the hedge may not match the duration of the related liability;
- certain types of hedges may expose us to risk of loss beyond the fee paid to initiate the hedge;
-

the amount of gross income that a REIT may earn from certain hedging transactions is limited by federal income tax provisions governing REITs;

- 40 -

- the credit quality of the counterparty on the hedge may be downgraded to such an extent that it impairs our ability to sell or assign our side of the hedging transaction; and
- the counterparty in the hedging transaction may default on its obligation to pay.

There are no perfect hedging strategies, and interest rate hedging may fail to protect us from loss. Alternatively, we may fail to properly assess a risk to our investment portfolio or may fail to recognize a risk entirely, leaving us exposed to losses without the benefit of any offsetting hedging activities. The derivative financial instruments we select may not have the effect of reducing our interest rate risk. The nature and timing of hedging transactions may influence the effectiveness of these strategies. Poorly designed strategies or improperly executed transactions could actually increase our risk and losses. In addition, hedging activities could result in losses if the event against which we hedge does not occur.

Because of the foregoing risks, our hedging activity could materially adversely affect our business, financial condition and results of operation and our ability to pay distributions to our stockholders.

Our use of certain hedging techniques may expose us to counterparty risks.

If an interest rate swap counterparty cannot perform under the terms of the interest rate swap, we may not receive payments due under that swap, and thus, we may lose any unrealized gain associated with the interest rate swap. The hedged liability could cease to be hedged by the interest rate swap. Additionally, we may also risk the loss of any collateral we have pledged to secure our obligations under the interest rate swap if the counterparty becomes insolvent or files for bankruptcy. Similarly, if an interest rate cap counterparty fails to perform under the terms of the interest rate cap agreement, we may not receive payments due under that agreement that would off-set our interest expense and then could incur a loss for the then remaining fair market value of the interest rate cap.

Hedging instruments often are not traded on regulated exchanges, guaranteed by an exchange or a clearing house, or regulated by any U.S. or foreign governmental authorities and involve risks and costs.

The cost of using hedging instruments increases as the period covered by the instrument increases and during periods of rising and volatile interest rates. We may increase our hedging activity and thus increase our hedging costs during periods when interest rates are volatile or rising and hedging costs have increased.

In addition, hedging instruments involve risk since they often are not traded on regulated exchanges, guaranteed by an exchange or its clearing house, or regulated by any U.S. or foreign governmental authorities. While the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act, or the Dodd-Frank Act, among other current or proposed pieces of legislation, may add regulatory oversight or reduce counterparty risk among market participants, little of such oversight currently exists. Consequently, there are no requirements with respect to record keeping, financial responsibility or segregation of customer funds and positions. Furthermore, the enforceability of agreements underlying derivative transactions may depend on compliance with applicable statutory and commodity and other regulatory requirements and, depending on the identity of the counterparty, applicable international requirements. The business failure of a hedging counterparty with whom we enter into a hedging transaction most likely will result in a default. Default by a hedging counterparty may result in the loss of unrealized profits and force us to cover our resale commitments, if any, at the then current market price. In addition, we may not always be able to dispose of or close out a hedging position without the consent of the hedging counterparty, and we may not be able to enter into an offsetting contract to cover our risk. We cannot assure you that a liquid secondary market will exist for hedging instruments purchased or sold, and we may be required to maintain a position until exercise or expiration, which could materially adversely affect our business, financial condition and results of operations and our ability to pay

distributions to our stockholders.

- 41 -

We may change our investment strategy, investment guidelines and asset allocation without notice or stockholder consent, which may result in riskier investments. In addition, our charter provides that our Board of Directors may revoke or otherwise terminate our REIT election, without the approval of our stockholders.

Our Board of Directors has the authority to change our investment strategy or asset allocation at any time without notice to or consent from our stockholders. To the extent that our investment strategy changes in the future, we may make investments that are different from, and possibly riskier than, the investments described in this prospectus. A change in our investment strategy may increase our exposure to interest rate and real estate market fluctuations. Furthermore, a change in our asset allocation could result in our allocating assets in a different manner than as described in this annual report.

In addition, our charter provides that our Board of Directors may revoke or otherwise terminate our REIT election, without the approval of our stockholders, if it determines that it is no longer in our best interests to qualify as a REIT. These changes could materially adversely affect our business, financial condition, results of operations, the market value of our common stock and our ability to make distributions to our stockholders.

Competition might prevent us from acquiring Agency MBS at favorable yields, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We operate in a highly competitive market for investment opportunities. Our net income largely depends on our ability to acquire Agency MBS at favorable spreads over our borrowing costs. In acquiring Agency MBS, we compete with a variety of institutional investors, including other REITs, investment banking firms, savings and loan associations, banks, insurance companies, mutual funds, other lenders and other entities that purchase Agency MBS, many of which have greater financial, technical, marketing and other resources than we do. Several other REITs have recently raised, or are expected to raise, significant amounts of capital, and may have investment objectives that overlap with ours, which may create additional competition for investment opportunities. Some competitors may have a lower cost of funds and access to funding sources that may not be available to us, such as funding from the U.S. Government. Additionally, many of our competitors are not subject to REIT tax compliance or required to maintain an exemption from the Investment Company Act. In addition, some of our competitors may have higher risk tolerances or different risk assessments, which could allow them to consider a wider variety of investments. Furthermore, competition for investments in Agency MBS may lead the price of such investments to increase, which may further limit our ability to generate desired returns. As a result, we may not be able to acquire sufficient Agency MBS at favorable spreads over our borrowing costs, which would materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

The recent actions of the U.S. Government for the purpose of stabilizing the financial markets may adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

The U.S. Government, through the Federal Reserve, the U.S. Treasury, the SEC, the Federal Housing Administration, or FHA, the Federal Deposit Insurance Corporation, or FDIC, and other governmental and regulatory bodies have taken or are considering taking various actions to address the financial crisis. For example, on July 21, 2010, President Obama signed into law the Dodd-Frank Act. Many aspects of the Dodd-Frank Act are subject to rulemaking and will take effect over several years, making it difficult to anticipate the overall financial impact on us and, more generally, the financial services and mortgage industries. Additionally, we cannot predict whether there will be additional proposed laws or reforms that would affect us, whether or when such changes may be adopted, how such changes may be interpreted and enforced or how such changes may affect us. However, the costs of complying with any additional laws or regulations could have a material adverse effect on our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

In addition to the foregoing, the U.S. Congress and/or various state and local legislatures may enact additional legislation or regulatory action designed to address the current economic crisis or for other purposes that could have a material adverse effect on our ability to execute our business strategies. To the extent the market does not respond favorably to these initiatives or they do not function as intended, our business, financial condition and results of operations and our ability to pay distributions to our stockholders could be materially adversely affected.

Terrorist attacks and other acts of violence or war may materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We cannot assure you that there will not be further terrorist attacks against the United States or U.S. businesses. These attacks or armed conflicts may directly impact the property underlying our Agency MBS or the securities markets in general. Losses resulting from these types of events are uninsurable. More generally, any of these events could cause consumer confidence and spending to decrease or result in increased volatility in the United States and worldwide financial markets and economies. They also could result in economic uncertainty in the United States or abroad. Adverse economic conditions could harm the value of the property underlying our Agency MBS or the securities markets in general, which could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We are highly dependent on communications and information systems operated by third parties, and systems failures could significantly disrupt our business, which may, in turn, adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

Our business is highly dependent on communications and information systems that allow us to monitor, value, buy, sell, finance and hedge our investments. These systems are operated by third parties and, as a result, we have limited ability to ensure their continued operation. In the event of a systems failure or interruption, we will have limited ability to affect the timing and success of systems restoration. Any failure or interruption of our systems could cause delays or other problems in our securities trading activities, including Agency MBS trading activities, which could have a material adverse effect on our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

If we issue debt securities, our operations may be restricted and we will be exposed to additional risk.

If we decide to issue debt securities in the future, it is likely that such securities will be governed by an indenture or other instrument containing covenants restricting our operating flexibility. Additionally, any convertible or exchangeable securities that we issue in the future may have rights, preferences and privileges more favorable than those of our Class A Common Stock. We, and indirectly our stockholders, will bear the cost of issuing and servicing such securities. Holders of debt securities may be granted specific rights, including but not limited to, the right to hold a perfected security interest in certain of our assets, the right to accelerate payments due under the indenture, rights to restrict dividend payments, and rights to approve the sale of assets. Such additional restrictive covenants and operating restrictions could have a material adverse effect on our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We depend primarily on two individuals to operate our business, and the loss of one or both of such persons could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

We depend substantially on two individuals, Robert E. Cauley, our Chairman and Chief Executive Officer, and G. Hunter Haas, our President, Chief Investment Officer and Chief Financial Officer, to manage our business. We depend on the diligence, experience and skill of Mr. Cauley and Mr. Haas in managing all aspects of our business, including the selection, acquisition, structuring and monitoring of securities portfolios and associated borrowings. Although we have entered into contracts and compensation arrangements with Mr. Cauley and Mr. Haas that encourage their continued employment, those contracts may not prevent either Mr. Cauley or Mr. Haas from leaving our company. The loss of either of them could materially adversely affect our business, financial condition and results of operations and our ability to pay distributions to our stockholders.

No assurance can be given that the Securities and Exchange Commission will not alter or eliminate the exemption available to the Company under Section 3(c)(5)(C) of the Investment Company Act of 1940. Should the exemption be eliminated, the Company's use of leverage would be limited to 50% of net assets. The Company currently generates a material portion of its net interest income from the application of leverage through repurchase agreement funding to its pass-through sub-portfolio. Should the exemption be withdrawn, the Company's ability to generate sufficient net interest income to cover its expenses would be impaired.

On August 31, 2011, the Securities and Exchange Commission (the "SEC") issued a Concept release (File No. S7-34-11) regarding "Companies Engaged in the Business of Acquiring Mortgages and Mortgage-Related Instruments". The SEC has requested public comment on the exemption from the definition of "investment company" contained in Section 3(c)(5)(C) of the Investment Company Act of 1940. The Company relies on this exemption in order to apply leverage via repurchase agreement funding to its sub-portfolio of pass-through securities. The net interest income generated by the levered pass-through sub-portfolio is a material component of the Company's strategy of generating net interest income to cover its expenses and generate dividends for its shareholders. The SEC release was published in early September 2011, and provided for a public comment period that ended on November 7, 2011. The SEC is currently considering what changes or clarifications, if any, should be made to the exemption under the Investment Company Act of 1940. At this time the Company is unable to determine what changes to the exemption, if any, will be made, and if changes to the exemption do occur, what impact will it have of the Company's results of operations.

LEGAL AND TAX RISKS

If we fail to qualify as a REIT, we will be subject to federal income tax as a regular corporation and may face a substantial tax liability.

We intend to operate in a manner that allows us to qualify as a REIT for federal income tax purposes. However, REIT qualification involves the satisfaction of numerous requirements (some on an annual or quarterly basis) established under technical and complex provisions of the Code, as amended, or regulations under the Code, for which only a limited number of judicial or administrative interpretations exist. The determination that we qualify as a REIT requires an analysis of various factual matters and circumstances that may not be totally within our control. For instance, a lack of access to adequate financing may prevent us from maintaining a portfolio of sufficient size to satisfy the REIT qualification requirements. Such could be the case when market conditions become severely distressed and/or the Company's financial condition deteriorates materially. Accordingly, it is not certain we will be able to qualify and remain qualified as a REIT for federal income tax purposes. Even a technical or inadvertent violation of the REIT requirements could jeopardize our REIT qualification. Furthermore, Congress or the Internal Revenue Service, or IRS, might change the tax laws or regulations and the courts might issue new rulings, in each case potentially having a

retroactive effect that could make it more difficult or impossible for us to qualify as a REIT. If we fail to qualify as a REIT in any tax year, then:

- 44 -

- we would be taxed as a regular domestic corporation, which, among other things, means that we would be unable to deduct distributions to stockholders in computing taxable income and would be subject to federal income tax on our taxable income at regular corporate rates;
- any resulting tax liability could be substantial and would reduce the amount of cash available for distribution to stockholders, and could force us to liquidate assets at inopportune times, causing lower income or higher losses than would result if these assets were not liquidated; and
- unless we were entitled to relief under applicable statutory provisions, we would be disqualified from treatment as a REIT for the subsequent four taxable years following the year during which we lost our REIT qualification, and our cash available for distribution to its stockholders therefore would be reduced for each of the years in which we do not qualify as a REIT.

Even if we remain qualified as a REIT, we may face other tax liabilities that reduce our cash flow. We may also be subject to certain federal, state and local taxes on our income and property. Any of these taxes would decrease cash available for distribution to our stockholders.

Complying with REIT requirements may cause us to forego otherwise attractive opportunities.

To qualify as a REIT for federal income tax purposes, we must continually satisfy tests concerning, among other things, our sources of income, the nature and diversification of our assets, the amounts we distribute to our stockholders and the ownership of our stock. We may also be required to make distributions to our stockholders at unfavorable times or when we do not have funds readily available for distribution. Thus, compliance with REIT requirements may hinder our ability to operate solely with the goal of maximizing profits.

In addition, the REIT provisions of the Code impose a 100% tax on income from "prohibited transactions." Prohibited transactions generally include sales of assets that constitute inventory or other property held for sale to customers in the ordinary course of business, other than foreclosure property. This 100% tax could impact our ability to sell mortgage-related securities at otherwise opportune times if we believe such sales could result in our being treated as engaging in prohibited transactions. However, we would not be subject to this tax if we were to sell assets through a taxable REIT subsidiary. We will also be subject to a 100% tax on certain amounts if the economic arrangements between us and our taxable REIT subsidiary are not comparable to similar arrangements among unrelated parties.

Complying with REIT requirements may limit our ability to hedge effectively, which could in turn leave us more exposed to the effects of adverse changes in interest rates.

The REIT provisions of the Code may substantially limit our ability to hedge mortgage-related securities and related borrowings by generally requiring us to limit our income in each year from qualified hedges, together with any other income not generated from qualified REIT real estate assets, to less than 25% of our gross income. In addition, we must limit our aggregate gross income from non-qualified hedges, fees, and certain other non-qualifying sources, to less than 5% of our annual gross income. As a result, we may in the future have to limit the use of hedges or implement hedges through a taxable REIT subsidiary. This could result in greater risks associated with changes in interest rates than we would otherwise want to incur. If we fail to satisfy the 25% or 5% limitations, unless our failure was due to reasonable cause and not due to willful neglect and we meet certain other technical requirements, we could lose our REIT qualification. Even if our failure was due to reasonable cause, we may have to pay a penalty tax equal to the amount of income in excess of certain thresholds, multiplied by a fraction intended to reflect our profitability.

Dividends paid by REITs are not qualified dividends eligible for reduced tax rates.

In general, the current maximum federal income tax rate for “qualified dividends” paid to individual U.S. stockholders is 15%. Dividends paid by REITs, however, are generally not qualified dividends eligible for the reduced rates. The more favorable rates applicable to regular corporate dividends, which are usually qualified dividends, could cause stockholders who are individuals to perceive investments in REITs to be relatively less attractive than investments in the stock of non-REIT corporations that pay dividends, which could adversely affect the value of the stock of REITs, including our Class A Common Stock.

To maintain our REIT qualification, we may be forced to borrow funds on unfavorable terms or sell our MBS portfolio securities at unfavorable prices to make distributions to our stockholders.

As a REIT, we must distribute at least 90% of our annual net taxable income (excluding net capital gains) to our stockholders. To the extent that we satisfy this distribution requirement, but distribute less than 100% of our net taxable income, we will be subject to federal corporate income tax. In addition, we will be subject to a 4% nondeductible excise tax if the actual amount that we pay to our stockholders in a calendar year is less than a minimum amount specified under the Code. From time to time, we may generate taxable income greater than our income for financial reporting purposes from, among other things, amortization of capitalized purchase premiums, or our net taxable income may be greater than our cash flow available for distribution to our stockholders. If we do not have other funds available in these situations, we could be required to borrow funds, sell a portion of our mortgage-related securities at unfavorable prices or find other sources of funds in order to meet the REIT distribution requirements and to avoid corporate income tax and the 4% excise tax. These other sources could increase our costs or reduce equity and reduce amounts available to invest in mortgage-related securities.

Reliance on legal opinions or statements by issuers of mortgage-related securities could result in a failure to comply with REIT gross income or asset tests.

When purchasing mortgage-related securities, we may rely on opinions of counsel for the issuer or sponsor of such securities, or statements made in related offering documents, for purposes of determining whether and to what extent those securities constitute REIT real estate assets for purposes of the REIT asset tests and produce income which qualifies under the REIT gross income tests. The inaccuracy of any such opinions or statements may adversely affect our REIT qualification and could result in significant corporate-level tax.

Possible legislative or other actions affecting REITs could adversely affect us and our stockholders.

The rules dealing with federal income taxation are constantly under review by persons involved in the legislative process and by the IRS and the U.S. Treasury Department. Our business may be harmed by changes to the laws and regulations affecting us, including changes to securities laws and changes to the Code provisions applicable to the taxation of REITs. New legislation may be enacted into law, or new interpretations, rulings or regulations could be adopted, any of which could adversely affect us and our stockholders, potentially with retroactive effect.

We may recognize excess inclusion income that would increase the tax liability of our stockholders.

If we recognize excess inclusion income and that is allocated to our stockholders, this income cannot be offset by net operating losses of our stockholders. If the stockholder is a tax-exempt entity, then this income would be fully taxable as unrelated business taxable income under Section 512 of the Code. If the stockholder is a foreign person, such income would be subject to federal income tax withholding without reduction or exemption pursuant to any otherwise applicable income tax treaty. In addition, to the extent our stock is owned by tax-exempt "disqualified organizations," such as government-related entities that are not subject to tax on unrelated business taxable income, although Treasury regulations have not yet been drafted to clarify the law, we may incur a corporate level tax at the highest applicable corporate tax rate on the portion of our excess inclusion income that is allocable to such disqualified organizations.

Excess inclusion income could result if we hold a residual interest in a real estate mortgage investment conduit, or REMIC. Excess inclusion income also could be generated if we were to issue debt obligations with two or more maturities and the terms of the payments on these obligations bore a relationship to the payments received on our mortgage-related securities securing those debt obligations (i.e., if we were to own an interest in a taxable mortgage pool). However, Treasury regulations have not been issued regarding the allocation of excess inclusion income to stockholders of a REIT that owns an interest in a taxable mortgage pool. We do not expect to acquire significant amounts of residual interests in REMICs, other than interests already owned by our taxable REIT subsidiary, which is treated as a separate taxable entity for these purposes. We intend to structure borrowing arrangements in a manner designed to avoid generating significant amounts of excess inclusion income. We do, however, expect to enter into various repurchase agreements that have differing maturity dates and afford the lender the right to sell any pledged mortgaged securities if we should default on our obligations.

A portion of our distributions may be deemed a return of capital for U.S. federal income tax purposes.

The amount of our distributions to the holders of our Class A Common Stock in a given year may not correspond to REIT taxable income for that year. To the extent our distributions exceed our REIT taxable income, the distribution will be treated as a return of capital for federal income tax purposes. A return of capital distribution will not be taxable to the extent of a stockholder's tax basis in our shares but will reduce a stockholder's basis in our shares of Class A Common Stock.

Our reported GAAP financial results differ from the taxable income results that drive our dividend distributions.

Our dividend distributions are driven by the dividend distribution requirements under the REIT tax laws and our profits as calculated for tax purposes pursuant to the Code. Our reported results for GAAP purposes may differ materially from both our cash flows and our REIT taxable income. As a result of the significant differences between GAAP and REIT taxable income accounting, stockholders and analysts must undertake a complex analysis to understand our tax results and dividend distribution requirements. This complexity may hinder the trading of our stock or may lead observers to misinterpret our results.

Legislation related to corporate governance has increased our costs of compliance and our liability.

Enacted and proposed laws, regulations and standards relating to corporate governance and disclosure requirements applicable to public companies, including the Sarbanes-Oxley Act of 2002, have increased the costs of corporate governance, reporting and disclosure practices. These costs may increase in the future due to our continuing implementation of compliance programs mandated by these requirements. In addition, these new laws, rules and regulations create new legal bases for administrative enforcement, civil and criminal proceedings against us in case of non-compliance, thereby increasing our risks of liability and potential sanctions.

Failure to maintain an exemption from the Investment Company Act would harm our results of operations.

We intend to conduct our business so as not to become regulated as an investment company under the Investment Company Act. If we fail to qualify for this exemption, our ability to use leverage would be substantially reduced and we would be unable to conduct our business. The Investment Company Act exempts entities that are primarily engaged in the business of purchasing or otherwise acquiring mortgages and other liens on, and interests in, real estate. Under the current interpretation of the SEC staff, in order to qualify for this exemption, we must maintain at least 55% of our assets directly in these qualifying real estate interests, with at least 25% of remaining assets invested in real estate-related securities. Mortgage-related securities that do not represent all of the certificates issued with respect to an underlying pool of mortgages may be treated as separate from the underlying mortgage loans and, thus, may not qualify for purposes of the 55% requirement. Therefore, our ownership of these mortgage-related securities is limited by the provisions of the Investment Company Act.

In satisfying the 55% requirement under the Investment Company Act, we treat as qualifying interests mortgage-related securities issued with respect to an underlying pool as to which we hold all issued certificates. If the SEC or its staff adopts a contrary interpretation of such treatment, we could be required to sell a substantial amount of our mortgage-related securities under potentially adverse market conditions. Further, in order to ensure that we at all times qualify for the exemption under the Investment Company Act, we may be precluded from acquiring mortgage-related securities whose yield is higher than the yield on mortgage-related securities that could be purchased in a manner consistent with the exemption. These factors may increase our net loss.

MortCo may be obligated to repurchase certain mortgage loans it originated if applicable underwriting requirements were not satisfied. Such repurchases could adversely affect the financial condition of MortCo and further limit its ability to repay amounts owed to us.

Prior to ceasing its operations in April 2007, MortCo originated residential mortgage loans. Those loans were typically sold to Fannie Mae, and the related mortgage servicing rights were typically sold to third-party servicing companies. Fannie Mae, servicing companies and certain investors have made repurchase claims to MortCo regarding certain residential mortgage loans that were originated by MortCo. These claims generally result from a default by a borrower under a loan followed by a rescission of mortgage insurance coverage due to an alleged underwriting deficiency. If MortCo is required to repurchase loans or pay losses incurred by Fannie Mae, servicing companies, investors or other third parties on a significant number of loans, then the financial condition of MortCo and its already limited ability to repay debt that it owes to us will be adversely affected.

There may be a limited market for our Class A Common Stock in the future.

Until November 5, 2007, our Class A Common Stock was traded on the NYSE Euronext. Currently our Class A Common Stock is traded on the OTC bulletin board under the symbol "BMNM.OB". We may apply to list our Class A Common Stock on another national securities market in the future; however, no assurance can be given that our Class A Common Stock will be approved for listing on such national securities market. Until such time that our Class A Common Stock is approved for listing on another national securities market, the ability to buy and sell our Class A Common Stock may be limited, and significant sales may depress or result in a decline in the market price of our Class A Common Stock. Additionally, until such time that our Class A Common Stock is approved for listing on another national securities market, our ability to raise capital through the sale of additional securities may be limited.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

Our executive offices and principal administrative offices are located at 3305 Flamingo Drive, Vero Beach, Florida, 32963, in an office building which we own. This property is suitable and adequate for our business as currently conducted.

ITEM 3. LEGAL PROCEEDINGS.

We are involved in various lawsuits and claims, both actual and potential, including some that we have asserted against others, in which monetary and other damages are sought. Except as described below, these lawsuits and claims relate primarily to contractual disputes arising out of the ordinary course of our business. The outcome of such lawsuits and claims is inherently unpredictable. However, we believe that, in the aggregate, the outcome of all lawsuits and claims involving us will not have a material effect on our consolidated financial position or liquidity; however, any such outcome may be material to the results of operations of any particular quarterly reporting period in which costs, if any, are recognized. See also Note 12 to our accompanying consolidated financial statements.

A complaint by a note-holder in Preferred Term Securities XX (“PreTSL XX”) was filed on July 16, 2010 in the Supreme Court of the State of New York, New York County, against Bimini Capital Management, Inc. (“Bimini”), the Bank of New York Mellon (“BNYM”), PreTSL XX, Ltd. and Hexagon Securities, LLC (“Hexagon”). The complaint, filed by Hildene Capital Management, LLC and Hildene Opportunities Fund, Ltd. (“Hildene”), alleges that Hildene suffered losses as a result of Bimini’s repurchase of all outstanding fixed/floating rate capital securities of Bimini Capital Trust II for less than par value from PreTSL XX in October 2009. Hildene has alleged claims against BNYM for breach of the Indenture, breach of fiduciary duties and breach of covenant of good faith and fair dealing, and claims against Bimini for tortious interference with contract, aiding and abetting breach of fiduciary duty, unjust enrichment and “rescission/illegality”. Plaintiff also alleges derivative claims brought in the name of Nominal Defendant BNYM. (On May 2, 2011, Hexagon and Nominal Defendant PreTSL XX were voluntarily dismissed without prejudice by Hildene.) On May 23, 2011, Bimini and BNYM moved to dismiss Hildene’s derivative claims, and Bimini also moved to dismiss Hildene’s claim for “rescission/illegality.” On October 19, 2011, PreTSL XX moved to intervene as an additional plaintiff in the action, and Bimini and BNYM have opposed that motion. Bimini denies that the repurchase was improper and intends to defend the suit vigorously.

On June 14, 2007, a complaint was filed in the Circuit Court of the Twelfth Judicial District in and for Manatee County, Florida by Coast Bank of Florida against MortCo seeking monetary damages and specific performance and alleging breach of an alleged oral contract for allegedly failing to convert approximately fifty construction loans to permanent financing. A non-jury trial was scheduled to begin on January 17, 2012. However, on January 16, 2012 the parties entered into a settlement agreement. Pursuant to the settlement agreement, MortCo, without admitting any allegations, paid Coast \$800,000 and the litigation and all related claims were dismissed with prejudice. Each party is responsible for the payment of its own legal fees and expenses.

On March 2, 2011, MortCo and Opteum Mortgage Acceptance Corporation (“Opteum Acceptance”) (referred to together herein as “MortCo”) received a cover letter dated March 1, 2011 from Massachusetts Mutual Life Insurance Company (“Mass Mutual”) enclosing a draft complaint against MortCo. In summary, Mass Mutual alleges that it purchased residential mortgage-backed securities offered by MortCo in August 2005 and the first quarter of 2006 and that MortCo made false representations and warranties in connection with the sale of the securities in violation of Mass Gen. Laws Ch. 110A § 410(a)(2) (the “Massachusetts Blue Sky Law”). In its cover letter, Mass Mutual claims it is entitled to damages in excess of \$25 million. However, no monetary demand is contained within the enclosed draft complaint and the actual damages Mass Mutual claims to have incurred is uncertain.

Mass Mutual has not filed the complaint or initiated litigation. Pursuant to its request, on March 14, 2011 Mass Mutual and MortCo entered into a Tolling Agreement through June 1, 2011 so that Mass Mutual could address its allegations against MortCo without incurring litigation costs. Mass Mutual has not yet contacted MortCo to schedule such discussions. On August 22, 2011, the parties extended the Tolling Agreement through June 1, 2013.

- 49 -

MortCo denies it made false representations and warranties in connection with the sale of securities to Mass Mutual. Mass Mutual has taken no action to prosecute its claim against MortCo, and the range of loss or potential loss, if any, cannot reasonably be estimated. Should Mass Mutual initiate litigation, MortCo will defend such litigation vigorously.

ITEM 4. MINE SAFETY DISCLOSURE

Not Applicable.

- 50 -

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES.

MARKET INFORMATION

Our Class A Common Stock is traded over-the-counter under the symbol "BMNM.OB". As of December 31, 2011, we had 10,086,854 shares of Class A Common Stock outstanding, which were held by approximately 406 holders of record. The 406 holders of record include Cede & Co., which holds shares as nominee for The Depository Trust Company, which itself holds shares for the benefit of 72 beneficial owners of our Class A Common Stock.

The following table is a summary of historical price information and dividends declared and paid per common share. Over-the-counter quotations reflect inter-dealer prices, without retain mark-up, mark-down or commission and may not necessarily represent actual transactions. All amounts have been adjusted for the March 12, 2010 reverse stock split.

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter	Full Year
2011					
High	\$0.98	\$0.89	\$0.85	\$0.75	\$0.98
Low	0.71	0.68	0.30	0.25	0.25
Close	0.77	0.73	0.61	0.37	0.37
Dividends declared per share	-	0.0325	0.0325	-	0.0650
2010					
High	\$3.00	\$1.74	\$1.01	\$0.95	\$3.00
Low	0.80	0.74	0.77	0.74	0.74
Close	0.99	0.94	0.84	0.78	0.78
Dividends declared per share	-	0.0600	-	0.0625	0.1225

As of December 31, 2011, we had 31,938 shares of Class B Common Stock outstanding, which were held by 2 holders of record and 31,938 shares of Class C Common Stock outstanding, which were held by one holder of record. There is no established public trading market for our Class B Common Stock or Class C Common Stock.

DIVIDEND DISTRIBUTION POLICY

In order to maintain our qualification as a REIT under the Code, we must make distributions to our stockholders each year in an amount at least equal to:

• 90% of our REIT taxable income (computed without regard to our deduction for dividends paid and our net capital gains);

• plus 90% of the excess of net income from foreclosure property over the tax imposed on such income by the Code;

- minus any excess non-cash income that exceeds a percentage of our income.

In general, our distributions will be applied toward these requirements if paid in the taxable year to which they relate, or in the following taxable year if the distributions are declared before we timely file our tax return for that year, the distributions are paid on or before the first regular distribution payment following the declaration, and we elect on our tax return to have a specified dollar amount of such distributions treated as if paid in the prior year. Distributions declared by us in October, November or December of one taxable year and payable to a stockholder of record on a specific date in such a month are treated as both paid by us and received by the stockholder during such taxable year, provided that the distribution is actually paid by us by January 31 of the following taxable year.

We anticipate that distributions generally will be taxable as ordinary income to our stockholders, although a portion of such distributions may be designated by us as capital gain or may constitute a return of capital. We furnish annually to each of our stockholders a statement setting forth distributions paid during the preceding year and their characterization as ordinary income, return of capital or capital gains.

EQUITY COMPENSATION PLAN INFORMATION

The plan documents for the plans described in the footnotes below are included as Exhibits to this Form 10-K, and are incorporated herein by reference in their entirety. The following table provides information as of December 31, 2011 regarding the number of shares of Class A Common Stock that may be issued under our equity compensation plans.

Plan Category	Total number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders (1)	367,844 (2)	-	4,956,404 (3)
Equity compensation plans not approved by security holders	-	-	-
Total	367,844	-	4,956,404

(1) Equity compensation plans approved by shareholders include the Bimini Capital Management, Inc. 2003 Long Term Incentive Plan (the "2003 Plan") and the Bimini Capital Management, Inc. 2011 Long Term Incentive Compensation Plan (the "2011 Plan"). The 2003 plan was approved by shareholders on December 18, 2003, prior to our initial public offering. The 2011 Plan was approved by shareholders on August 12, 2011. Both plans are broad-based equity incentive plans that permit the grant of stock options, restricted stock, phantom shares, dividend equivalent rights and other stock-based awards. Subject to adjustment upon certain corporate transactions or events, a maximum of 1,448,050 shares of Class A Common Stock (but no more than 10% of the number of shares of Class A Common Stock outstanding on any particular grant date) may be subject to awards under the 2003 Plan. Subject to adjustment upon certain transactions or events, a maximum of 4,000,000 shares of Class A Common Stock (but no more than 10% of the number of shares of Class A Common Stock outstanding on any particular grant date) may be subject to awards under the 2011 Plan.

(2)

Represents the aggregate number of shares of Class A Common Stock remaining to be issued upon settlement of phantom share awards granted pursuant to the 2003 Plan and outstanding as of December 31, 2011. As of December 31, 2011, no shares have been awarded under the 2011 Plan.

- (3) Represents the maximum number of shares remaining available for future issuance under the terms of the 2003 and 2011 plans irrespective of the 10% limitation described in footnote 1 above. Taking into account the 10% limitation and the number of shares of Class A Common Stock outstanding as of December 31, 2011, there were no additional shares remaining available for future issuance under the terms of the 2003 Plan and, 1,008,686 shares are available for future issuance under the terms of the 2011 Plan as of December 31, 2011.

UNREGISTERED SALES OF EQUITY SECURITIES

During the year ended December 31, 2011, the Company issued 179,180 and 118,743 shares of Class A Common Stock to Robert J. Dwyer and Frank E. Jaumot, respectively, in consideration for their service on the Company's Board of Directors and on certain committees of the Board of Directors. The shares were issued pursuant to the exemption from registration under the Securities Act of 1933, as amended, contained in Section 4(2) thereof.

ISSUER PURCHASES OF EQUITY SECURITIES

The Company did not repurchase any shares of its stock during the three months ended December 31, 2011.

ITEM 6. SELECTED FINANCIAL DATA

Not Applicable.

- 53 -

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

FORWARD-LOOKING STATEMENTS

When used in this Annual Report on Form 10-K, in future filings with the SEC or in press releases or other written or oral communications, statements which are not historical in nature, including those containing words such as "anticipate," "estimate," "should," "expect," "believe," "intend" and similar expressions, are intended to identify "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act").

These forward-looking statements are subject to various risks and uncertainties, including, but not limited to, those described or incorporated by reference in "Part I - Item 1A - Risk Factors" of this Form 10-K. These and other risks, uncertainties and factors, including those described in reports that the Company files from time to time with the Commission, could cause the Company's actual results to differ materially from those reflected in such forward-looking statements. All forward-looking statements speak only as of the date they are made and the Company does not undertake, and specifically disclaims, any obligation to update or revise any forward-looking statements to reflect events or circumstances occurring after the date of such statements.

The following discussion of the financial condition and results of operations should be read in conjunction with the Company's consolidated financial statements and related notes included elsewhere in this report.

INTRODUCTION

As used in this document, references to "Bimini Capital," the parent company, the registrant, and to real estate investment trust ("REIT") qualifying activities or the general management of Bimini Capital's portfolio of MBS refer to "Bimini Capital Management, Inc." and its wholly-owned qualified REIT subsidiary, Orchid Island Capital, Inc. ("Orchid"). Further, references to Bimini Capital's taxable REIT subsidiaries or non-REIT eligible assets refer to Bimini Advisors, Inc. ("Bimini Advisors") and to MortCo TRS, LLC ("MortCo") and its consolidated subsidiaries. MortCo, which was previously named Opteum Financial Services, LLC, (referred to as "OFS") was renamed Orchid Island TRS, LLC (referred to as "OITRS") effective July 3, 2007 and then renamed MortCo TRS, LLC effective March 8, 2011. Hereinafter, any historical mention, discussion or references to Opteum Financial Services, LLC, Orchid Island TRS, LLC, OFS or to OITRS (such as in previously filed documents or Exhibits) now means MortCo. References to the "Company" refer to the consolidated entity which is the combination of Bimini Capital, Orchid, Bimini Advisors, MortCo and MortCo's consolidated subsidiaries.

Bimini Capital was formed in September 2003 to invest primarily in but not limited to, residential mortgage related securities issued by the Federal National Mortgage Association (more commonly known as Fannie Mae), the Federal Home Loan Mortgage Corporation (more commonly known as Freddie Mac) and the Government National Mortgage Association (more commonly known as Ginnie Mae). Bimini Capital will deploy its capital into two core strategies. The two strategies are a levered MBS portfolio and an unlevered structured MBS portfolio. The leverage applied to the MBS portfolio will typically be less than twelve to one. Bimini Capital manages its portfolio of agency MBS and structured MBS to generate income derived from the net interest margin of its MBS portfolio, levered predominantly under repurchase agreement funding, net of associated hedging costs, and the interest income derived from its unlevered portfolio of structured MBS. Bimini Capital treats its remaining junior subordinated notes as an equity capital equivalent. Bimini Capital is self-managed and self-advised and has elected to be taxed as a REIT for U.S. federal income tax purposes.

On April 18, 2007, the Board of Managers of MortCo, at the recommendation of the Board of Directors of the Company, approved the closure of the wholesale and conduit mortgage loan origination channels. Both channels ceased accepting new applications for mortgage loans on April 20, 2007. On May 7, 2007, MortCo signed a binding agreement, later amended, to sell its retail mortgage loan origination channel to a third party. The transaction closed on June 30, 2007 and MortCo has not operated a mortgage loan origination business since that date. Since the second quarter of 2007, through September 30, 2010, MortCo was reported as a discontinued operation following applicable accounting standards, since most of the remaining assets and liabilities were considered to be contingent and were held by MortCo pursuant to the terms of the disposal of the operations. The disposal of the retained interests asset was not achieved as a result of the lingering effects of the financial market crisis and a significant lack of investor interest in such securities, even though the Company made efforts to market such securities to previously active market participants. Because MortCo continued to hold these net assets, the remnants of the old mortgage banking business were no longer classified as discontinued operations effective October 1, 2010, and the related assets and liabilities previously classified as held for sale were reclassified to held and used for all periods presented.

DIVIDENDS TO STOCKHOLDERS

In order to maintain its qualification as a REIT, Bimini Capital is required (among other provisions) to annually distribute dividends to its stockholders in an amount at least equal to, generally, 90% of Bimini Capital's REIT taxable income. REIT taxable income is a term that describes Bimini Capital's operating results calculated in accordance with rules and regulations promulgated pursuant to the Internal Revenue Code.

Bimini Capital's REIT taxable income is computed differently from net income as computed in accordance with generally accepted accounting principles ("GAAP net income"), as reported in the Company's accompanying consolidated financial statements. Depending on the number and size of the various items or transactions being accounted for differently, the differences between REIT taxable income and GAAP net income can be substantial and each item can affect several reporting periods. Generally, these items are timing or temporary differences between years; for example, an item that may be a deduction for GAAP net income in the current year may not be a deduction for REIT taxable income until a later year. The most significant differences are as follows: the results of the Company's taxable REIT subsidiaries do not impact REIT taxable income, unrealized gains or losses on the investment securities portfolio do not impact REIT taxable income, and interest income on MBS securities is computed differently for REIT taxable income and GAAP.

As a REIT, Bimini Capital may be subject to a federal excise tax if Bimini Capital distributes less than 85% of its REIT taxable income by the end of the calendar year. Accordingly, Bimini Capital's dividends are based on its REIT taxable income (after considering the possible impact of applying NOLs to the income as described below in "Net Operating Losses"), as determined for federal income tax purposes, as opposed to its net income computed in accordance with GAAP (as reported in the accompanying consolidated financial statements).

During the year ended December 31, 2011, the Company paid distributions of \$0.065 per share on a loss of \$0.26 per share. These distributions were funded by cash on hand and cash flows generated from the Company's investment portfolio. While the Company intends to pay quarterly distributions to our stockholders such that substantially all of our REIT taxable income is distributed, it has not established a minimum distribution payout level and the ability to pay distributions may be adversely affected by a variety of factors. All distributions will be made at the discretion of the Company's Board of Directors and will depend on the Company's results of operations, financial conditions, maintenance of REIT status and other factors that may be deemed relevant; therefore, distributions may be reduced or eliminated at any time. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Outlook" below for additional information regarding distributions.

In August 2011, the Company announced that, based on results of operations through June 30, 2011, it would suspend its quarterly dividend until at least early 2012. For the year ended December 31, 2011, the Company generated a REIT taxable loss. The Company will re-evaluate its dividend payment policy during 2012.

- 55 -

NET OPERATING LOSSES

As described above, a REIT may be subject to a federal excise tax if it distributes less than 85% of its REIT taxable income by the end of a calendar year. In calculating the amount of excise tax payable in a given year, if any, Bimini Capital reduces REIT taxable income by distributions made to stockholders in the form of dividends and/or net operating losses (“NOL’s”) applied from prior years, to the extent any are available. Since income subject to excise tax is REIT taxable income less qualifying dividends and the application of NOL’s, a REIT may avoid excise taxes solely by application of available NOL’s without paying qualifying dividends to stockholders. Because Bimini Capital currently has \$10.6 million of NOL’s available, in the future it could avoid excise taxes by applying such NOL’s to offset REIT taxable income without making any distributions to stockholders. Further, the REIT could avoid the obligation to pay excise taxes through a combination of qualifying dividends and the application of NOL’s. In any case, future distributions to stockholders may be less than taxable income until the existing NOL’s are consumed.

RESULTS OF OPERATIONS

Described below are the Company’s results of operations for the year ended December 31, 2011, as compared to the Company’s results of operations for the year ended December 31, 2010.

Net Loss Summary

Consolidated net loss for the year ended December 31, 2011 was \$2.6 million, or \$0.26 basic and diluted loss per share of Class A Common Stock, as compared to consolidated net loss of \$1.7 million, or \$0.18 basic and diluted loss per share of Class A Common Stock, for the year ended December 31, 2010.

The components of net loss for the years ended December 31, 2011 and 2010, along with the changes in those components are presented in the table below:

(in thousands)

	Years Ended December 31,		
	2011	2010	Change
Net portfolio interest	\$4,816	\$6,189	\$(1,373)
Interest expense on junior subordinated notes	(1,008)	(2,118)	1,110
Losses on MBS and Eurodollar futures	(1,939)	(864)	(1,075)
Net portfolio income	1,869	3,207	(1,338)
Other income	3,125	2,722	403
Expenses	(7,616)	(7,821)	205
Income tax benefit	-	145	(145)
Net loss	\$(2,622)	\$(1,747)	\$(875)

Net Portfolio Income

During the year ended December 31, 2011, the REIT generated \$4.8 million of net portfolio interest income, consisting of \$5.1 million of interest income from MBS assets offset by \$0.27 million of interest expense on repurchase liabilities. For the comparable period ended December 31, 2010, the REIT generated \$6.2 million of net portfolio interest income, consisting of \$6.5 million of interest income from MBS assets offset by \$0.28 million of interest expense on repurchase liabilities.

The table below provides information on our portfolio average balances, interest income, yield on assets, average repurchase agreement balances, interest expense, cost of funds, net interest income and net interest rate for each quarter in 2011 and 2010 and for the years ended December 31, 2011 and 2010.

(dollars in thousands)

	Average MBS Securities Held	Interest Income	Yield on Average MBS Securities		Average Repurchase Agreements	Interest Expense	Average Cost of Funds		Net Portfolio Interest Income	Net Interest Spread	
Three Months Ended,											
December 31, 2011	\$89,670	\$1,039	4.64 %	\$	68,462	\$59	0.35 %	\$	980	4.29 %	
September 30, 2011	101,102	1,133	4.48 %	\$	79,750	53	0.26 %	\$	1,080	4.22 %	
June 30, 2011	115,521	1,301	4.51 %	\$	93,516	72	0.31 %	\$	1,229	4.20 %	
March 31, 2011	126,084	1,608	5.10 %	\$	104,259	87	0.33 %	\$	1,521	4.77 %	
December 31, 2010	132,955	1,496	4.50 %	\$	110,433	88	0.32 %	\$	1,408	4.18 %	
September 30, 2010	114,165	1,260	4.42 %	\$	89,440	69	0.31 %	\$	1,191	4.11 %	
June 30, 2010	99,856	1,807	7.24 %	\$	74,163	53	0.29 %	\$	1,754	6.95 %	
March 31, 2010	110,914	1,896	6.84 %	\$	88,495	68	0.31 %	\$	1,828	6.53 %	
Years Ended,											
December 31, 2011	\$108,094	\$5,081	4.70 %	\$	86,497	\$271	0.31 %	\$	4,810	4.39 %	
December 31, 2010	114,473	6,459	5.64 %	\$	90,633	278	0.31 %	\$	6,181	5.34 %	

Interest income presented in the table above includes only interest earned on the Company's MBS investments and excludes interest earned on cash balances. Interest income and net portfolio interest income may not agree with the information presented in the income statement. Portfolio yields and costs of borrowings presented in the table above and the tables on pages 58 and 59 are calculated based on the average balances of the underlying investment portfolio/repurchase agreement balances and are annualized for the quarterly periods presented. Average balances for quarterly periods are calculated using two data points, the beginning and ending balances. Average balances for the year to date periods are calculated as the average of the average quarterly periods.

Interest Income and Average Earning Asset Yield

Interest income was \$5.1 million for the year ended December 31, 2011 and \$6.5 million for the year ended December 31, 2010. Average MBS holdings were \$108.1 million and \$114.5 million for the years ended December 31, 2011 and 2010, respectively. The \$1.4 million decrease in interest income was due to a 94 basis point decrease in yields, which was partially offset by a \$6.4 million decrease in average MBS holdings.

The table below presents the average portfolio size, income and yields of our respective sub-portfolios, consisting of structured MBS and PT MBS.

(dollars in thousands)

	Average MBS Held			Interest Income			Realized Yield on Average MBS					
	PT MBS	Structured MBS	Total	PT MBS	Structured MBS	Total	PT MBS	Structured MBS	Total			
Three Months Ended,												
December												
31, 2011	\$71,230	\$ 18,440	\$89,670	\$596	\$ 443	\$1,039	3.35	%	9.60	%	4.64	%
September												
30, 2011	83,004	18,098	101,102	588	545	1,133	2.84	%	12.03	%	4.48	%
June 30,												
2011	98,060	17,461	115,521	755	546	1,301	3.08	%	12.52	%	4.51	%
March 31,												
2011	108,382	17,702	126,084	927	681	1,608	3.42	%	15.39	%	5.10	%
December												
31, 2010	114,570	18,385	132,955	994	502	1,496	3.47	%	10.92	%	4.50	%
September												
30, 2010	93,579	20,586	114,165	833	427	1,260	3.56	%	8.31	%	4.42	%
June 30,												
2010	79,691	20,165	99,856	761	1,046	1,807	3.82	%	20.76	%	7.24	%
March 31,												
2010	94,493	16,421	110,914	1,048	848	1,896	4.44	%	20.64	%	6.84	%
Years Ended,												
December												
31, 2011	\$90,169	\$ 17,925	\$108,094	\$2,866	\$ 2,215	\$5,081	3.18	%	12.35	%	4.70	%
December												
31, 2010	95,583	18,890	114,473	3,635	2,824	6,459	3.80	%	14.95	%	5.64	%

Interest Expense on Repurchase Agreements and the Cost of Funds

Average outstanding repurchase agreements were \$86.5 million and total interest expense was \$0.27 million for the year ended December 31, 2011. During the year ended December 31, 2010, average outstanding repurchase agreements were \$90.6 million and total interest expense was \$0.28 million. Our average cost of funds was 0.31% for both the year ended December 31, 2011 and 2010. There was a \$0.01 million decrease in interest expense for the year ended December 31, 2011 when compared to the year ended December 31, 2010. This change was due entirely to a \$4.1 million decrease in average outstanding repurchase agreements for the year ended December 31, 2011 when compared to the same period ended December 31, 2010.

Since all of our repurchase agreements are short-term, changes in market rates directly affect our interest expense. Our average cost of funds was 9 basis points above average one-month LIBOR and 30 basis points below average six-month LIBOR for the quarter ended December 31, 2011. The average term to maturity of the outstanding repurchase agreements decreased from 28 days at December 31, 2010 to 25 days at December 31, 2011.

The Company has not elected to designate its derivative holdings, specifically, its investment in Eurodollar futures contracts for hedge accounting treatment under the Financial Accounting Standards Board (the "FASB") Accounting

Standards Codification (“ASC”) Topic 815, Derivatives and Hedging. Changes in fair value of these investments are presented in a separate line item in the Company’s Consolidated Statements of Operations. As such, for financial reporting purposes, interest expense and cost of funds are not impacted by the Company’s investment in Eurodollar futures contracts.

- 58 -

(dollars in thousands)

	Average Balance of		Average Cost of Funds	Average		Average		Average Cost of Funds Relative to Average		Average Cost of Funds Relative to Average	
	Repurchase Agreements	Interest Expense		One-Month LIBOR	Six-Month LIBOR	One-Month LIBOR	Six-Month LIBOR	One-Month LIBOR	Six-Month LIBOR		
Three Months Ended,											
December 31, 2011	\$68,462	\$59	0.35 %	0.26 %	0.65 %	0.09 %	(0.30) %				
September 30, 2011	79,750	53	0.26 %	0.21 %	0.46 %	0.05 %	(0.20) %				
June 30, 2011	93,516	72	0.31 %	0.22 %	0.43 %	0.09 %	(0.12) %				
March 31, 2011	104,259	87	0.33 %	0.26 %	0.46 %	0.07 %	(0.13) %				
December 31, 2010	110,433	88	0.32 %	0.26 %	0.47 %	0.06 %	(0.15) %				
September 30, 2010	89,440	69	0.31 %	0.30 %	0.61 %	0.01 %	(0.30) %				
June 30, 2010	74,163	53	0.29 %	0.29 %	0.58 %	0.00 %	(0.29) %				
March 31, 2010	88,495	68	0.31 %	0.24 %	0.43 %	0.07 %	(0.12) %				
Years Ended,											
December 31, 2011	\$86,497	\$271	0.31 %	0.24 %	0.50 %	0.07 %	(0.19) %				
December 31, 2010	90,633	278	0.31 %	0.27 %	0.52 %	0.04 %	(0.21) %				

Junior Subordinated Notes

Interest expense on the Company's junior subordinated debt securities was \$1.0 million for the year ended December 31, 2011 compared to \$2.1 million for the comparable period in 2010. The junior subordinated debt securities had a fixed-rate of interest until December 15, 2010, of 7.86% and thereafter, through maturity in 2035, the rate floats at a spread of 3.50% over the prevailing three-month LIBOR rate. As of December 31, 2011, the interest rate was 4.05%. The average rate of interest paid, including the amortization of debt issuance costs, for the year ended December 31, 2011 was 3.88% compared to 8.15% for the comparable period in 2010. Interest expense decreased \$1.1 million for the year ended December 31, 2011 when compared to the same period in 2010 due to the 427 basis point decrease in interest rates, and amortization of debt issuance costs during the 2010 period.

Gains and Losses

The table below presents the Company's gains and losses for the year ended December 31, 2011 and 2010.

(in thousands)

	Years Ended December 31,		
	2011	2010	Change

Realized gains on sales of MBS	\$941	\$786	\$155
Fair value adjustments on MBS	(1,786)	(1,258)	(528)
Total losses on MBS	(845)	(472)	(373)
Losses on Eurodollar futures	(1,094)	(392)	(702)
Gains on residual interests	3,190	2,216	974

During the years ended December 31, 2011 and 2010, the Company received proceeds of \$95.4 million and \$105.2 million, respectively, from the sales of MBS.

The retained interests in securitizations represent residual interests in loans originated or purchased by MortCo prior to securitization. Fluctuations in value of retained interests are primarily driven by projections of future interest rates (the forward LIBOR curve), the discount rate used to determine the present value of the residual cash flows and prepayment and loss estimates on the underlying mortgage loans.

Operating Expenses

For the year ended December 31, 2011, Bimini Capital's total operating expenses were approximately \$7.6 million, compared to approximately \$7.8 million for the year ended December 31, 2010. The table below provides a breakdown of operating expenses for the years ended December 31, 2011 and 2010.

During the second quarter of 2011, the Company took steps related to a proposed public offering of Orchid common stock. The offering was expected to be completed in July 2011. However, Orchid withdrew its S-11 Registration Statement related to the offering during the third quarter of 2011. The Registration Statement was withdrawn due to several market factors, including the Federal debt ceiling extension crisis that played out in Congress in late July and early August of 2011. Included in other professional fees for the year ended December 31, 2011 are approximately \$1.1 million of expenses related to this attempted public offering.

In January 2012, MortCo settled certain litigation as further described in Note 12 to the financial statements. Included in other G&A expenses for the year ended December 31, 2011 is \$800,000 related to this settlement.

As described in Note 6 to the financial statements, one of the Company's repurchase agreement counterparties, MF Global, Inc., filed for bankruptcy protection on October 31, 2011. Included in other administrative expenses for the year ended December 31, 2011 is a \$300,000 reserve the Company has established against amounts due from this counterparty.

(in thousands)

	Years Ended December 31,		
	2011	2010	Change
Direct REIT operating expenses	\$542	\$595	\$(53)
Compensation and benefits	1,514	1,976	(462)
Legal fees	1,539	2,700	(1,161)
Accounting, auditing and other professional fees	1,691	580	1,111
Directors' fees and liability insurance	587	517	70
Other G&A expenses	1,744	1,453	291
	\$7,617	\$7,821	(204)

Financial Condition:

Mortgage-Backed Securities

As of December 31, 2011, the MBS portfolio consisted of \$91.1 million of agency or government MBS at fair value and had a weighted average coupon on assets of 4.37%. During the year ended December 31, 2011, we received principal repayments of \$25.4 million compared to \$33.1 million for the year ended December 31, 2010. The average prepayment speeds for the quarters ended December 31, 2011 and 2010 were 31.1% and 28.3%, respectively. (See table below for additional prepayment data).

The following table presents the constant prepayment rate (“CPR”) experienced on our structured and pass-through (“PT”) MBS sub-portfolios, on an annualized basis, for the quarterly periods presented.

Three Months Ended,	PT MBS Portfolio	Structured MBS Portfolio	Total Portfolio
December 31, 2011	14.1	33.7	31.1
September 30, 2011	13.4	22.8	20.9
June 30, 2011	11.8	13.0	12.7
March 31, 2011	12.0	19.1	17.2
December 31, 2010	11.7	34.5	28.3
September 30, 2010	17.2	35.0	30.6
June 30, 2010	27.8	44.9	42.1
March 31, 2010	9.2	33.3	28.8

The following tables summarize certain characteristics of the Company’s agency and government mortgage related securities as of December 31, 2011 and 2010:

(in thousands)

Asset Category	Fair Value	Percentage of Entire Portfolio	Weighted Average Coupon	Weighted Average Maturity in Months	Longest Maturity	Weighted Average Reset in Months	Weighted Average Lifetime Cap	Weighted Average Periodic Cap	
December 31, 2011									
Adjustable Rate MBS	\$ 12,181	13.4%	2.89%	233	1-Jan-41	4.36	11.07%	2.00%	
Fixed Rate MBS	35,417	38.9%	4.84%	178	1-Nov-40	NA	NA	NA	
Hybrid Adjustable Rate MBS	25,466	27.9%	3.57%	354	1-Dec-41	95.21	8.83%	2.00%	
Total Mortgage-backed Pass-through	73,064	80.2%	4.07%	249	1-Dec-41	65.82	9.55%	2.00%	
Structured MBS	18,078	19.8%	5.61%	300	25-Nov-40	NA	NA	NA	
Total Mortgage Assets	\$ 91,142	100.0%	4.37%	259	1-Dec-41	NA	NA	NA	
December 31, 2010									
Adjustable Rate MBS	\$ 64,458	47.7%	2.83%	279	1-Jan-41	2.72	10.19%	2.00%	
Fixed Rate MBS	50,013	37.0%	4.90%	178	1-Apr-36	NA	NA	NA	
Hybrid Adjustable Rate MBS	2,783	2.1%	5.18%	295	1-Aug-35	18.03	10.18%	2.00%	
Total Mortgage-backed Pass-through	117,254	86.8%	3.77%	236	1-Jan-41	3.35	10.19%	2.00%	
Structured MBS	17,879	13.2%	5.83%	272	16-Nov-39	NA	NA	NA	
Total Mortgage Assets	\$ 135,133	100.0%	4.04%	241	1-Jan-41	3.35	NA	2.00%	

(in thousands)

Agency	Fair Value	December 31, 2011		December 31, 2010	
		Percentage of Entire Portfolio	Percentage of Entire Portfolio	Fair Value	Percentage of Entire Portfolio

Edgar Filing: BIMINI CAPITAL MANAGEMENT, INC. - Form 10-K

Fannie Mae	\$58,628	64.33	%	\$103,568	76.64	%
Freddie Mac	27,267	29.92	%	25,710	19.03	%
Ginnie Mae	5,247	5.76	%	5,855	4.33	%
Total Portfolio	\$91,142	100.00	%	\$135,133	100.0	%

- 61 -

	December 31, 2011	December 31, 2010
Entire Portfolio		
Weighted Average Pass Through Purchase Price	\$104.43	\$104.44
Weighted Average Structured Purchase Price	\$6.13	\$5.46
Weighted Average Pass Through Current Price	\$106.13	\$105.29
Weighted Average Structured Current Price	\$6.5	\$5.98
Effective Duration (1)	(3.492)	1.024

(1) Effective duration of (3.492) indicates that an interest rate increase of 1.0% would be expected to cause a 3.492% increase in the value of the MBS in the Company's investment portfolio at December 31, 2011. An effective duration of 1.024 indicates that an interest rate increase of 1.0% would be expected to cause a 1.024% decrease in the value of the MBS in the Company's investment portfolio at December 31, 2010. These figures include the structured securities in the portfolio.

The following table presents details related to portfolio assets acquired for the years ended December 31, 2011 and 2010.

(in thousands)

	2011			2010		
	Total Cost	Average Price	Weighted Average Yield	Total Cost	Average Price	Weighted Average Yield
Pass-through MBS	\$55,974	105.38	2.01 %	\$118,052	105.40	2.29 %
Structured MBS	21,606	11.32	16.13 %	36,046	9.71	21.50 %

The Company's portfolio of PT MBS will typically be comprised of adjustable-rate MBS, fixed-rate MBS and hybrid adjustable-rate MBS. The Company seeks to acquire low duration assets that offer high levels of protection from mortgage prepayments. Although the duration of an individual asset can change as a result of changes in interest rates, the Company strives to maintain a PT MBS portfolio with an effective duration of less than 2.0. The stated contractual final maturity of the mortgage loans underlying the Company's portfolio of PT MBS generally ranges up to 30 years. However, the effect of prepayments of the underlying mortgage loans tends to shorten the resulting cash flows from the Company's investments substantially. Prepayments occur for various reasons, including refinancing of underlying mortgages and loan payoffs in connection with home sales.

The duration of the Company's interest only ("IO") and inverse interest only ("IIO") portfolio will vary greatly owing to the structural features of the securities. While prepayment activity will always affect the cash flows associated with the securities, the interest only nature of IO's may cause their durations to become extremely negative when prepayments are high, and less negative when prepayments are low. With respect to IIO's, prepayments affect their durations in a similar fashion to that of IO's, but the floating rate nature of their coupon (which is inversely related to the level of one month LIBOR) cause their price movements – and model duration - to be affected by changes in both prepayments and one month LIBOR – both current and anticipated levels. As a result, the duration of IIO securities will also vary greatly.

Prepayments on the loans underlying the Company's MBS can alter the timing of the cash flows from the underlying loans to the Company. As a result, the Company gauges the interest rate sensitivity of its assets by measuring their effective duration. While modified duration measures the price sensitivity of a bond to movements in interest rates, effective duration captures both the movement in interest rates and the fact that cash flows to a mortgage related security are altered when interest rates move. Accordingly, when the contract interest rate on a mortgage loan is

substantially above prevailing interest rates in the market, the effective duration of securities collateralized by such loans can be quite low because of expected prepayments. Although some of the fixed-rate MBS in the Company's portfolio are collateralized by loans with a lower propensity to prepay when the contract rate is above prevailing rates, their price movements track securities with like contract rates and therefore exhibit similar effective duration.

- 62 -

The Company faces the risk that the market value of its assets will increase or decrease at different rates than that of its liabilities, including its hedging instruments. Accordingly, the Company assesses its interest rate risk by estimating the duration of its assets and the duration of its liabilities. The Company generally calculates duration using various third party models. However, empirical results and various third party models may produce different duration numbers for the same securities.

The following sensitivity analysis shows the estimated impact on the fair value of the Company's interest rate-sensitive investments as of December 31, 2011, assuming rates instantaneously fall 100 basis points ("bps"), rise 100 bps and rise 200 bps:

(in thousands)

	Fair Value	\$ Change in Fair Value			% Change in Fair Value			
		-100BPS	+100BPS	+200BPS	-100BPS	+100BPS	+200BPS	
Adjustable Rate MBS	\$12,181	\$78	\$(78)	\$(157)	0.64	% (0.64)	)(%) (1.29))(%)
Hybrid								
Adjustable Rate MBS	25,466	453	(453)	(906)	1.78	% (1.78)	)(%) (3.56))(%)
Fixed Rate MBS	35,417	734	(734)	(1,469)	2.07	% (2.07)	)(%) (4.15))(%)
Structured MBS	18,078	(4,448)	4,448	8,897	(24.61)	)(%) 24.61	% 49.21	%
Portfolio Total	\$91,142	\$(3,183)	\$3,183	\$6,365	(3.49)	)(%) 3.49	% 6.98	%

The table below reflects the same analysis presented above but with the figures in the columns that indicate the estimated impact of a 100 bps fall or rise adjusted to reflect the impact of convexity.

(in thousands)

	Fair Value	\$ Change in Fair Value			% Change in Fair Value			
		-100BPS	+100BPS	+200BPS	-100BPS	+100BPS	+200BPS	
Adjustable Rate MBS	\$12,181	\$105	\$(157)	\$(356)	0.86	% (1.29)	)(%) (2.92))(%)
Hybrid								
Adjustable Rate MBS	25,466	1,035	(1,532)	(3,216)	4.06	% (6.02)	)(%) (12.63))(%)
Fixed Rate MBS	35,417	774	(1,106)	(2,438)	2.19	% (3.12)	)(%) (6.88))(%)
Structured MBS	18,078	(2,406)	3,210	4,589	(13.31)	)(%) 17.76	% 25.39	%
Portfolio Total	\$91,142	\$(492)	\$415	\$(1,421)	(0.54)	)(%) 0.46	% (1.56))(%)

The Company has economically hedged a portion of its interest rate risk by entering into Eurodollar futures contracts. The Company did not elect hedging treatment under the applicable accounting standards, and as such, all gains and losses on these instruments are reflected in earnings. The table below reflects the impact on operations as of December 31, 2011, assuming rates fall 100 bps, rise 100 bps and rise 200 bps:

(in thousands)

	Notional Amount	\$ Change in Fair Value			% Change in Fair Value			
		-100BPS	+100BPS	+200BPS	-100BPS	+100BPS	+200BPS	
Repurchase Agreement								
Hedges	\$50,000	\$(423)	\$550	\$1,100	(0.77)	)(%) 1.01	% 2.02	%
	21,000	(397)	473	945	(0.85)	)(%) 1.01	% 2.02	%

Junior
Subordinated
Debt Hedges

Portfolio Total	\$71,000	\$(820)	\$1,023	\$2,045	(0.81)%	1.01	%	2.02	%
-----------------	----------	--------	---	---------	---------	-------	----	------	---	------	---

In addition to changes in interest rates, other factors impact the fair value of Bimini Capital's interest rate-sensitive investments and hedging instruments, such as the shape of the yield curve, market expectations as to future interest rate changes and other market conditions. Accordingly, in the event of changes in actual interest rates, the change in the fair value of Bimini Capital's assets would likely differ from that shown above and such difference might be material and adverse to Bimini Capital's stockholders.

- 63 -

Repurchase Agreements

As of December 31, 2011, the Company had established borrowing facilities in the repurchase agreement market with five counterparties which we believe provide borrowing capacity in excess of our needs. None of these lenders are affiliated with the Company. As of December 31, 2011, we had funding in place with three of those counterparties. These borrowings are secured by the Company's MBS and bear interest rates that are based on a spread to LIBOR.

As of December 31, 2011, the Company had obligations outstanding under the repurchase agreements of approximately \$69.5 million with a net weighted average borrowing cost of 0.43%. The remaining maturity of the Company's outstanding repurchase agreement obligations ranged from 4 to 30 days, with a weighted average maturity of 25 days. Securing the repurchase agreement obligation as of December 31, 2011, are MBS with an estimated fair value, including accrued interest, of \$73.3 million and a weighted average maturity of 249 months. Through March 9, 2012, the Company has been able to maintain its repurchase facilities with its counterparties with comparable terms to those that existed at December 31, 2011 with maturities through May 16, 2012.

On October 31, 2011, MF Global Holding Ltd. ("MF") filed for bankruptcy protection under Chapter 11 of the U.S. Bankruptcy Code. As of September 30, 2011, a subsidiary of MF, MF Global, Inc. was the Company's largest repurchase agreement funding provider and the Company had approximately \$2.3 million at risk under such agreements. As of December 31, 2011, the Company had no outstanding funding arrangements in place with MF under repurchase agreements. All repurchase agreements in place at September 30, 2011, have been terminated and all pledged assets have been returned. One reverse-repurchase agreement with MF has yet to be fully unwound and the Company has not received funds which are owed by MF to the Company in the amount of approximately \$343,000. At December 31, 2011, the Company established a reserve of \$300,000 against this balance. The Company believes it is entitled to these funds; however, given publicly-disclosed developments at MF and the fact that MF is in bankruptcy, it is not known if or when the funds will be received.

The table below presents information about our period end and average repurchase agreement obligations for each quarter in 2011 and 2010.

(dollars in thousands)

Three Months Ended,	Ending Balance of Repurchase Agreements	Average Balance of Repurchase Agreements	Difference Between Ending Repurchase Agreements and Average Repurchase Agreements	
			Amount	Percent
December 31, 2011	\$ 69,528	\$ 68,462	\$ 1,066	1.56%
September 30, 2011	67,396	79,750	(12,354)	(15.49%)(a)
June 30, 2011	92,105	93,516	(1,411)	(1.51)%
March 31, 2011	94,927	104,259	(9,332)	(8.95)%
December 31, 2010	113,592	110,433	3,159	2.86%
September 30, 2010	107,274	89,440	17,834	19.94%(b)
June 30, 2010	71,606	74,163	(2,557)	(3.45)%
March 31, 2010	76,719	88,495	(11,776)	(13.31%)(c)

(a) The lower ending balance relative to the average balance reflects a shift in the portfolio allocation towards assets that the Company does not fund through the repo market. During the quarter ended September 30, 2011, the Company's investment in PT MBS decreased \$27.2 million.

(b) The higher ending balance relative to the average balance reflects a shift in the portfolio allocation towards assets that the Company typically finances. During the quarter ended September 30, 2010, the investment in PT MBS increased \$36.6 million.

(c) The lower ending balance relative to the average balance reflects a shift in the portfolio allocation towards assets that the Company does not fund through the repo market. During the quarter ended March 31, 2010, the Company's investment in PT MBS decreased \$20.8 million.

Liquidity and Capital Resources

Liquidity is our ability to turn non-cash assets into cash, purchase additional investments, repay principal and interest on borrowings, fund overhead, fulfill margin calls and pay dividends. Our principal immediate sources of liquidity include cash balances, unencumbered assets and borrowings under repurchase agreements. Our borrowing capacity will vary over time as the market value of our interest earning assets varies. Our balance sheet also generates liquidity on an on-going basis through payments of principal and interest we receive on our MBS portfolio, and from cash flows received from the retained interests and the collection of servicing advances. Management believes that we currently have sufficient liquidity and capital resources available for (a) the acquisition of additional investments when considered appropriate, (b) the repayments on borrowings and (c) the payment of dividends to the extent required for Bimini's continued qualification as a REIT.

Because our PT MBS portfolio consists entirely of government and agency securities, we do not anticipate having difficulty converting our assets to cash should our liquidity needs ever exceed our immediately available sources of cash. Our structured MBS portfolio also consists of entirely governmental agency securities, although they typically do not trade with comparable bid / ask spreads as PT MBS. However, we anticipate that we would be able to liquidate such securities readily, even in distressed markets, albeit with potential haircuts.

Bimini Capital's master repurchase agreements have no stated expiration, but can be terminated at any time at Bimini Capital's option or at the option of the counterparty. However, once a definitive repurchase agreement under a master repurchase agreement has been entered into, it generally may not be terminated by either party. A negotiated termination can occur, but may involve a fee to be paid by the party seeking to terminate the repurchase agreement transaction.

At December 31, 2011, the weighted average haircut our repurchase agreement counterparties required us to hold was 5% of the estimated fair value of the underlying collateral.

Under our repurchase agreement funding arrangements we are required to post margin at the initiation of the borrowing. The margin posted represents the haircut, which is a percentage of the market value of the collateral pledged. To the extent the market value of the asset collateralizing the financing transaction declines, the market value of our posted margin will be insufficient and we will be required to post additional collateral. Conversely, if the market value of the asset pledged increases in value, we would be over collateralized and we could then call our repo counterparty and have excess margin returned to us. Our lenders typically value our pledged securities daily to ensure the adequacy of our margin and make margin calls as needed, as do we. Typically, but not always, the parties agree to a minimum threshold amount for margin calls so as to avoid the need for nuisance margin calls on a daily basis.

As a result of losses incurred during and after the period when MortCo operated a mortgage loan origination business, the Company was forced to materially downsize its investment portfolio to raise cash, and was left with a depleted capital base. This period covered the years 2006, 2007 and 2008. These losses reduced the Company's access to funding via repurchase agreements. In order to augment its existing leveraged MBS portfolio with alternative sources of income, the Company developed an alternative investment strategy utilizing structured MBS with comparable borrower and prepayment characteristics to the securities historically held in the portfolio. Such securities are not funded in the repurchase market but instead are purchased directly, thus reducing – but not eliminating - the Company's reliance on access to repurchase agreement funding. The leverage inherent in the securities replaces the leverage obtained by acquiring PT securities and funding them in the repurchase market. This structured MBS strategy is now a core element of the Company's overall investment strategy.

As of December 31, 2011, the Company had cash and cash equivalents of \$4.3 million. We generated cash flows of \$30.6 million from principal and interest payments on our MBS portfolio and \$3.6 million from retained interests during the year ended December 31, 2011. The table below summarizes the effect on our liquidity and cash flows from certain contractual obligations as of December 31, 2011.

(in thousands)

	Obligations Maturing				Total
	Within One Year	One to Three Years	Three to Five Years	More than Five Years	
Repurchase agreements	\$69,528	\$-	\$-	\$-	\$69,528
Interest expense on repurchase agreements(1)	46	-	-	-	46
Junior subordinated notes(2)	-	-	-	26,000	26,000
Interest expense on junior subordinated notes(1)	1,099	2,104	2,104	20,310	25,617
Totals	\$70,673	\$2,104	\$2,104	\$46,310	\$121,191

(1) Interest expense on repurchase agreements and junior subordinated notes are based on current interest rates as of December 31, 2011 and the remaining term of liabilities existing at that date.

(2) The Company holds a common equity interest in Bimini Capital Trust II. The amount presented represents the net cash outlay of the Company.

In October 2005, Bimini Capital completed a private offering of \$51.5 million of trust preferred securities of Bimini Capital Trust II ("BCTII") resulting in the issuance by Bimini Capital of an additional \$51.5 million of junior subordinated notes. On October 21, 2009, the Company purchased \$24 million of trust preferred capital securities issued by BCT II. The total cost for the transaction, including fees was approximately \$14.5 million. The Company cancelled the trust preferred capital securities and the \$24.74 million of its junior subordinated notes issued to BCT II. As of December 31, 2011, \$26.8 million of the trust preferred securities of BCT II remain outstanding.

Outlook

The current growth rate of the U.S. economy has not been sufficient to allow the Federal Reserve to remove accommodations made available to the economy, namely low levels of the Federal Funds rate. This directly impacts the funding levels available to the Company. The low funding rate levels have enabled the Company to continue to generate net interest margins ("NIM") above our historical average.

Nonetheless, the reduced size of the portfolio in relation to the Company's operating expenses will constrain the earnings potential of the Company until assets under management can be increased. Given the reduced size of our portfolio, even with the benefit of its alternative investment strategy, no assurance can be made of the Company's ability to generate sufficient net interest income to cover all of its costs. The Company's ability to generate sufficient net interest income to cover its fixed and variable operating costs will also be impacted by funding costs, which in turn will depend on how long funding rates will remain at current low levels.

For the year ended December 31, 2011, Bimini Capital generated a REIT taxable loss. As more fully described in footnote 13 to the accompanying financial statements, REIT taxable income or loss generated by qualifying REIT activities is computed in accordance with the Internal Revenue Code, which is different from the Company's financial statement income or loss as computed in accordance with GAAP. In addition, Bimini Capital presently has REIT tax net operating loss carryovers of approximately \$10.6 million as of December 31, 2011 which are available to offset

future REIT taxable income. Distributions in the amount of \$0.065 per share paid to shareholders during 2011 will be considered a return-of-capital, which depletes the Company's capital base. Distributions made by the Company during 2010 were also a return-of-capital.

- 66 -

The Company has used the term “REIT taxable income” throughout this document as being the amount available for distribution to its stockholders before any NOLs are applied, and before any distributions. In arriving at income that could be subjected to taxation at the REIT entity level for a given year, dividends paid in the current year and any NOL’s from prior periods applied are deducted (in that order) from current period income first. Net operating losses expire 20 years from the year they are incurred. Since the REIT currently has NOL’s from prior periods available to offset income in future periods, the Company has the option, but not the obligation, to apply such NOL’s against income in future years. As a result, the REIT could have income in future years, but not make distributions to shareholders. This would occur if the REIT had sufficient NOL’s available to entirely offset the REIT income earned in a given year and chose to apply such NOL’s. The Company could also apply available NOL’s against future period earnings and reduce distributions to shareholders assuming the available NOL was less than the current period earnings.

Based on the factors described above, and in order to preserve its capital base, in August 2011, the Company opted to terminate its stock repurchase plan and, for the foreseeable future, suspend its quarterly distribution to stockholders. The Company will reevaluate its ability to resume distributions in 2012.

Recent Developments – HARP (Home Affordable Refinancing Program)

Last Fall the Federal Housing Finance Agency (FHFA), Fannie Mae and Freddie Mac announced changes to the Home Affordable Refinancing Program (HARP) which became effective on December 1, 2011. The changes to the program were designed to increase the number of loans currently eligible to be refinanced under existing guidelines and extend the term of the program through the end of 2013. The changes to the plan were initially announced on October 24, 2011, and final changes were announced on November 15, 2011. The changes to the original HARP program are expected to increase refinancing activity of eligible loans – predominantly fixed rate mortgages with higher coupons (ranging from 5.5% to 6.5%) originated between 2006 and 2008. Only loans originated before May 31, 2009 are eligible for refinancing under HARP. Further, the Obama Administration has stated it intends to continue to take steps to expand refinancing programs to borrowers, especially those who owe more on their home than it is worth. We do not know at this time what additional programs will result from these efforts, if any. Management is unable to predict the impact, if any, that the new HARP program terms, or terms of other yet unknown programs, will have on the Company’s portfolio and results of operations.

The table below provides details of the securities in our two portfolios that are eligible to be refinanced under the HARP guidelines:

(\$ in thousands)

	Market Value of Securities where Underlying Pools were issued Prior to May 31, 2009						Total Securities in Sub-Portfolio
	Underlying Current Gross WAC (Borrower Mortgage Rate)						
	Less Than 4.00%	4.0% - 4.99 %	5.0%-5.99 %	6.0% - 6.99 %	Greater Than 7.0%	Total	
Pass-through portfolio	\$9,367	\$-	\$4,199	\$5,012	\$-	\$18,578	\$ 73,064
Structured security portfolio	\$168	\$629	\$3,780	\$5,228	\$-	\$9,805	\$ 18,078
Total	\$9,535	\$629	\$7,979	\$10,240	\$-	\$28,383	\$ 91,142

Percent of Securities where Underlying Pools were Issued Prior to May 31, 2009

	Less Than 4.00%	4.0% - 4.99 %	5.0%-5.99 %	6.0% - 6.99 %	Greater Than	Total

7.0%

Pass-through portfolio	13	%	-	6	%	7	%	-	25	%	
Structured security portfolio	1	%	3	%	21	%	29	%	-	54	%
Total	10	%	1	%	9	%	11	%	-	31	%

- 67 -

Critical Accounting Policies

Management's discussion and analysis of financial condition and results of operations is based on the amounts reported in our financial statements. These financial statements are prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). The Company's significant accounting policies are described in Note 1 to the Company's accompanying Consolidated Financial Statements.

GAAP requires the Company's management to make various judgments, estimates and assumptions. Changes in these estimates and assumptions could have a material effect on our financial statements.

MORTGAGE-BACKED SECURITIES

The Company has elected to account for its investment in MBS under the fair value option. Changes in fair value of securities held for trading are recorded through the statement of operations. Our MBS are valued using Level 2 valuations, and such valuations currently are determined by the Company based on the average of third-party broker quotes and/or by independent pricing sources when available. Because the price estimates may vary, the Company must make certain judgments and assumptions about the appropriate price to use to calculate the fair values. Alternatively, the Company could opt to have the value of all of our positions in MBS determined by either an independent third-party or do so internally. In managing our portfolio, the Company employs the following four-step process at each valuation date to determine the fair value of our MBS:

- First, the Company obtains fair values from a subscription-based independent pricing source through our repurchase agreement funding services provider. These prices are used by both the Company as well as our repurchase agreement counterparty on a daily basis to establish margin requirements for our borrowings. As of June 30, 2011, the Company subscribed to a second subscription-based pricing service.
- Second, the Company requests non-binding quotes from one to four broker-dealers for each of its MBS in order to validate the values obtained by the pricing service. The Company requests these quotes from broker-dealers that actively trade and make markets in the respective asset class for which the quote is requested.
- Third, the Company reviews the values obtained by the pricing source and the broker-dealers for consistency across similar assets.
- Finally, if the data from the pricing services and broker-dealers is not homogenous or if the data obtained is inconsistent with management's market observations, the Company makes a judgment to determine which price appears the most consistent with observed prices from similar assets and selects that price. To the extent management believes that none of the prices are consistent with observed prices for similar assets, which is typically the case for only an immaterial portion of our portfolio each quarter, the Company may use a third price that is consistent with observed prices for identical or similar assets. In the case of assets that have quoted prices such as Agency MBS backed by fixed-rate mortgages, the Company generally uses the quoted or observed market price. For assets such as Agency MBS backed by ARMs or structured Agency MBS, the Company may determine the price based on the yield or spread that is identical to an observed transaction or a similar asset for which a dealer mark or subscription-based price has been obtained.

REPURCHASE AGREEMENTS

We finance the acquisition of our PT MBS through the use of repurchase agreements. Repurchase agreements are treated as collateralized financing transactions and are carried at their contractual amounts, including accrued interest,

as specified in the respective agreements.

- 68 -

INCOME RECOGNITION

All securities are either PT MBS securities, IO securities or IIO securities. Income on PT MBS securities is based on the stated interest rate of the security. Premium or discount present at the date of purchase is not amortized. For IIO and IO securities, the income is accrued based on the carrying value and the effective yield. As cash is received it is first applied to accrued interest and then to reduce the carrying value. At each reporting date, the effective yield is adjusted prospectively from the reporting period based on the new estimate of prepayments. The new effective yield is calculated based on the carrying value at the end of the previous reporting period, the new prepayment estimates and the contractual terms of the security. Changes in fair value during the period are recorded in earnings and reported as (losses) gains on mortgage-backed securities in the accompanying consolidated statement of operations.

INCOME TAXES

Bimini Capital has elected to be taxed as a REIT under the Code. As further described below, Bimini Capital's TRSs, MortCo and Bimini Advisors are taxpaying entities for income tax purposes and are taxed separately from Bimini Capital. Bimini Capital will generally not be subject to federal income tax on its REIT taxable income (net of the application of net operating loss carryovers) to the extent that Bimini Capital distributes its REIT taxable income to its stockholders and satisfies the ongoing REIT requirements, including meeting certain asset, income and stock ownership tests. A REIT must generally distribute at least 90% of its REIT taxable income to its stockholders, of which 85% generally must be distributed within the taxable year, in order to avoid the imposition of an excise tax. The remaining balance may be distributed up to the end of the following taxable year, provided the REIT elects to treat such amount as a prior year distribution and meets certain other requirements.

MortCo, Advisors and their activities are subject to corporate income taxes and the applicable provisions of FASB ASC Topic 740, Income Taxes. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. To the extent management believes deferred tax assets will not be fully realized in future periods, a provision is recorded so as to reflect the net portion, if any, of the deferred tax asset management expects to realize.

Off-Balance Sheet Arrangements

As discussed above, MortCo previously pooled loans that it had originated or purchased and then sold them or securitized them to obtain long-term financing for its assets. Securitized loans were transferred to a trust where they served as collateral for asset-backed bonds, which the trust primarily issued to the public. MortCo held approximately \$3.5 million of retained interests from securitizations as of December 31, 2011. In addition, MortCo retained the servicing related to the loans sold or securitized. While such servicing has been sold and or surrendered, advances made prior to such transactions continue to be collected as the underlying properties are liquidated.

The cash flows associated with MortCo's securitization activities for the years ended December 31, 2011 and 2010, were as follows:

(in thousands)

	Years Ended December 31,	
	2011	2010
Net servicing repayments	\$921	\$2,041
Cash flows received on retained interests	3,622	4,222

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Not Applicable.

- 69 -

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA.

Index to Financial Statements

	Page
Report of Independent Registered Public Accounting Firm	71
Consolidated Balance Sheets at December 31, 2011 and 2010	72
Consolidated Statements of Operations for the years ended December 31, 2011 and 2010	73
Consolidated Statements of Stockholders' Equity for the years ended December 31, 2011 and 2010	74
Consolidated Statements of Cash Flows for the years ended December 31, 2011 and 2010	75
Notes to Consolidated Financial Statements	76

Report of Independent Registered Public Accounting Firm

Board of Directors and Stockholders
Bimini Capital Management, Inc.
Vero Beach, Florida

We have audited the accompanying consolidated balance sheets of Bimini Capital Management, Inc. and subsidiaries (the "Company") as of December 31, 2011 and 2010 and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the two years in the period ended December 31, 2011. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company at December 31, 2011 and 2010, and the results of its operations and its cash flows for each of the two years in the period ended December 31, 2011, in conformity with accounting principles generally accepted in the United States of America.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the Company's internal control over financial reporting as of December 31, 2011, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated March 9, 2012 expressed an unqualified opinion thereon.

West Palm Beach, Florida
March 9, 2012

/s/ BDO USA, LLP
Certified Public Accountants

BIMINI CAPITAL MANAGEMENT, INC.
CONSOLIDATED BALANCE SHEETS

	December 31,	
	2011	2010
ASSETS:		
Mortgage-backed securities, at fair value		
Pledged to counterparties	\$73,064,201	\$117,253,931
Unpledged	18,078,052	17,879,409
Total mortgage-backed securities	91,142,253	135,133,340
Cash and cash equivalents	4,300,785	2,830,584
Restricted cash	417,000	3,545,885
Retained interests in securitizations	3,495,471	3,927,777
Accrued interest receivable	901,385	1,049,577
Property and equipment, net	3,884,056	3,894,717
Prepaid expenses and other assets, net	5,113,346	6,609,043
Total Assets	\$109,254,296	\$156,990,923
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES:		
Repurchase agreements, net	\$69,528,000	\$113,591,685
Junior subordinated notes due to Bimini Capital Trust II	26,804,440	26,804,440
Accrued interest payable	71,829	120,410
Accounts payable, accrued expenses and other	7,483,459	8,102,062
Total Liabilities	103,887,728	148,618,597
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; designated, 1,800,000 shares as Class A Redeemable and 2,000,000 shares as Class B Redeemable; no shares issued and outstanding as of December 31, 2011 and 2010	-	-
Class A Common Stock, \$0.001 par value; 98,000,000 shares designated: 10,086,854 shares issued and outstanding as of December 31, 2011 and 9,776,586 shares issued and outstanding as of December 31, 2010	10,087	9,777
Class B Common Stock, \$0.001 par value; 1,000,000 shares designated, 31,938 shares issued and outstanding as of December 31, 2011 and 2010	32	32
Class C Common Stock, \$0.001 par value; 1,000,000 shares designated, 31,938 shares issued and outstanding as of December 31, 2011 and 2010	32	32
Additional paid-in capital	334,075,197	334,459,072
Accumulated deficit	(328,718,780)	(326,096,587)
Total Stockholders' Equity	5,366,568	8,372,326
Total Liabilities and Stockholders' Equity	\$109,254,296	\$156,990,923

BIMINI CAPITAL MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,	
	2011	2010
Interest income	\$5,086,441	\$6,467,103
Interest expense	(270,787)	(278,060)
Net interest income, before interest on junior subordinated notes	4,815,654	6,189,043
Interest expense on junior subordinated notes	(1,007,603)	(2,118,486)
Net interest income	3,808,051	4,070,557
Losses on mortgage-backed securities	(845,439)	(471,708)
Losses on Eurodollar futures	(1,093,612)	(392,275)
Net portfolio income	1,869,000	3,206,574
Other income:		
Gains on retained interests in securitizations	3,189,844	2,215,739
Other (expense) income	(64,469)	506,556
Total other income	3,125,375	2,722,295
Expenses:		
Compensation and related benefits	1,513,729	1,976,019
Directors' fees and liability insurance	587,443	517,351
Audit, legal and other professional fees	3,230,130	3,280,422
Direct REIT operating expenses	541,758	594,719
Other administrative	1,743,508	1,452,889
Total expenses	7,616,568	7,821,400
Loss before income taxes	(2,622,193)	(1,892,531)
Income tax benefit	-	(145,000)
Net loss	\$(2,622,193)	\$(1,747,531)
Basic and Diluted Net loss Per Share of:		
CLASS A COMMON STOCK		
Basic and Diluted	\$(0.26)	\$(0.18)
CLASS B COMMON STOCK		
Basic and Diluted	\$(0.27)	\$(0.19)
Weighted Average Shares Outstanding:		
CLASS A COMMON STOCK		
Basic and Diluted	9,889,050	9,644,850
CLASS B COMMON STOCK		
Basic and Diluted	31,938	31,938
Dividends Declared Per Common Share:		
CLASS A COMMON STOCK	\$0.065	\$0.1225
CLASS B COMMON STOCK	\$0.065	\$0.1225

See Notes to Consolidated Financial Statements

BIMINI CAPITAL MANAGEMENT, INC.
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

	Common Stock, Amounts at par value			Additional Paid-in Capital	Accumulated Deficit	Total
	Class A	Class B	Class C			
Balances, January 1, 2010	\$2,764	\$32	\$32	\$319,191,227	\$(324,349,056)	\$(5,155,001)
Net loss	-	-	-	-	(1,747,531)	(1,747,531)
Dividends paid in shares of Class A						
Common Stock	7,241	-	-	16,647,596	-	16,654,837
Cash dividends declared	-	-	-	(1,276,929)	-	(1,276,929)
Issuance of Class A common shares for board compensation and equity plan exercises	176	-	-	160,162	-	160,338
Class A shares repurchased and retired	(404)	-	-	(348,940)	-	(349,344)
Amortization of equity plan compensation	-	-	-	85,956	-	85,956
Balances, December 31, 2010	\$9,777	\$32	\$32	\$334,459,072	\$(326,096,587)	\$8,372,326
Net loss	-	-	-	-	(2,622,193)	(2,622,193)
Cash dividends declared	-	-	-	(669,077)	-	(669,077)
Issuance of Class A common shares for board compensation and equity plan exercises	311	-	-	194,640	-	194,951
Class A shares repurchased and retired	(1)	-	-	(595)	-	(596)
Amortization of equity plan compensation	-	-	-	91,157	-	91,157
Balances, December 31, 2011	\$10,087	\$32	\$32	\$334,075,197	\$	